Service Date: October 31, 1997

DEPARTMENT OF PUBLIC SERVICE REGULATION
BEFORE THE PUBLIC SERVICE COMMISSION
OF THE STATE OF MONTANA

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IN THE MATTER OF MONTANA POWER COMPANY, Revenue Requirements, Gas Costs, Allocated Cost of Service and Rate Design for Natural Gas, Service, Restructuring, and Consolidation of Related Cases and Issues.	)	UTILITY DIVISION DOCKET NO. D96.2.22 ORDER NO. 5898d

FINAL ORDER

APPEARANCES

FOR THE APPLICANT:

Marjorie L. Thomas, Attorney at Law, Montana Power Co., 40 East Broadway, Butte, Montana 59701

FOR THE INTERVENORS:

Robert A. Nelson, Montana Consumer Counsel, 34 West Sixth Avenue, P.O. Box 201703, Helena, Montana 59620-1703

Donald W. Quander, Holland & Hart, LLP, P.O. Box 639, Billings, Montana 59103-0639, Attorneys at Law, for the Large Customer Group (ASARCO Inc., Ash Grove Cement, Conoco, Inc., Golden Sunlight Mines, Inc., Holnam, Inc., Montana Refining Company, Montana Tunnels Mining, Inc., and Stone Container Corp.)

Richard F. Gallagher, Church, Harris, Johnson & Williams, P.C., P.O. Box 1645, Great Falls, Montana 59403-1645, Attorneys at Law, for the Marketers (Energy West Resources, Interenergy, Eagle Gas Marketing / John O. Brown)

John C. Allen, Attorney at Law, Great Falls Gas Co., P.O. Box 2229, Great Falls, Montana 59403-2229, for Great Falls Gas Co.

Jim Madden, Attorney at Law, Montana Department of Environmental Quality, P.O. Box 200901, Helena, Montana 59620-0901, for the Department of Environmental Quality

Michael J. Uda, Doney, Crowley & Bloomquist, Attorneys at Law, P.O. Box 1185, Helena, Montana 59624-1185, for Paladin Associates and Ferdig Oil Company

Katharine S. Donnelley, Browning, Kaleczyc, Berry & Hoven, Attorneys at Law, P.O. Box 1697, Helena, Montana 59624, for MHA Ventures

Betsy R. Carr, Bracewell & Patterson, LLP, 2000 K Street, N.W., Suite 500, Washington, D.C., 20006, Attorney for Enron Capital and Trade Resources Corp.

Richard L. Beatty, Attorney at Law, P.O. Box 904, Shelby, Montana 59474, for Northern Montana Oil and Gas Association

FOR THE COMMISSION:

Martin Jacobson, Staff Attorney
Dan Elliott, Utility Division Administrator
Mike Lee, Economics and Rate Design Bureau Chief
Dave Burchett, Revenue Requirements Rate Analyst
Joel Tierney, Engineer / Revenue Requirements Rate Analyst

BEFORE:

DAVE FISHER, Chairman
NANCY MCCAFFREE, Vice Chair
BOB ANDERSON, Commissioner
DANNY OBERG, Commissioner
BOB ROWE, Commissioner

I. INTRODUCTION

1. On February 20, 1996, the Montana Public Service Commission (PSC or Commission) issued an "Order Initiating Proceeding" (Order No. 5898) commencing the above-entitled matter, directing Montana Power Company (MPC or Company), a public utility offering natural gas services to consumers within Montana, to prepare and file a comprehensive case regarding those services. There were several purposes underlying the required filing, the most notable ones being: to provide a means to resolve issues raised but unlikely to be resolved in several then-pending MPC gas or gas-related cases (e.g., MPC's 1994 gas cost tracker Docket No. 94.11.50, MPC's 1995 gas cost tracker Docket No. D95.12.166, and MPC's 1995 general rate case Docket No. D95.9.128); to prompt MPC to file an allocated cost of service and rate design

(ACOS/RD) case for its gas services; and to establish a procedure or forum to accommodate expressed interests in a comprehensive MPC gas case, particularly those interests concerned with restructuring MPC's gas utility (unbundling MPC's bundled gas service to allow for competition in supply, removing the commodity component from the customary "bundled" utility services and making it available on a competitive basis) through lowering or eliminating MPC's existing 60,000 mcf-per-year threshold to qualify for gas transportation service (established in PSC Docket No. 90.1.1, Order No. 5454c, October 3, 1991).

2. On July 29, 1996, MPC made the PSC-directed filing, presenting a revenue requirements increase, a gas tracker update, an allocated cost of service/rate design study, its position on issues deferred from the previous dockets, and a plan to restructure. An annual revenue increase of $4.85 million was proposed. The restructuring plan featured a reduction in the transportation threshold, pilot programs to introduce aggregation to residential and commercial customers, removal of MPC gas production assets from the regulated utility rate base and transfer of these assets into an unregulated energy supply division, the development of a universal system benefit program, and a mechanism for collecting stranded regulatory assets and stranded costs associated with gas production.

3. MPC's filing was publicly noticed and a procedural order was issued. Intervention was requested and granted. The active intervenors in the case include: the Montana Consumer Counsel (MCC); the Montana Large Customer Group (LCG) (including ASARCO Inc., Ash Grove Cement, Conoco, Inc., Golden Sunlight Mines, Inc., Holnam, Inc., Montana Refining Company, Montana Tunnels Mining, Inc., and Stone Container Corp.); certain Montana marketers (including Interenergy Corp., Energy West Resources, and Eagle Gas Marketing / John O. Brown); Great Falls Gas Co. (GFG); the Montana Department of Environmental Quality (DEQ); Human Resources Council District IX (HRC), Paladin Associates (PA); Ferdig Oil Co. (Ferdig); MHA Ventures, Inc. (MHA) (hospital members of the Montana Hospital Association);

Enron Capital and Trade Resources Corp. (Enron); and the Northern Montana Oil and Gas Association (NMOGA).

4. By late November 1996 proceedings had progressed through discovery on MPC's prefiled testimony, MPC responses to that discovery, intervenor prefiled testimony, discovery on intervenor prefiled testimony, and responses to that discovery. MPC's prefiled rebuttal testimony was the next scheduled event. MPC had also filed testimony addressing "additional issues" identified by the PSC (interconnection and aggregation). In addition, MPC's 1996 gas cost tracker had been filed and consolidated into this case. Discovery on MPC's additional issue testimony and MPC's 1996 tracker was the next scheduled event for these issues.

5. By December 10, 1996, it was apparent that proposed legislation would likely be introduced before Montana's 55th Legislature (to convene in early January, 1997) regarding restructuring of electric and gas utilities. Restructuring was an important reason for MPC's comprehensive case to begin with and developed significantly more importance as this case progressed. The proposed restructuring legislation, if approved, would likely influence or even direct the outcome of one or more of the developing issues before the PSC. For this reason, and because it became apparent that settlement was being considered among MPC and all or the majority of the intervenors and might be reached on a number of issues, the PSC suspended proceedings to allow all parties to explore settlement.

6. Although short-lived reinstatements of the procedural schedule did occur, for all practical purposes the PSC's suspension of proceedings lasted from December 10, 1996, to June 27, 1997. During this period of suspension gas utility restructuring was ultimately approved (in the form of SB396), became law (Ch. 506, L. 1997, the "Natural Gas Utility Restructuring and Customer Choice Act"), effective May 2, 1997, and is now codified at secs. 69-3-1401 through 69-3-1409, MCA. As approved the legislation does eliminate, influence, or direct the outcome of the restructuring issues in this case.

7. Also during the period of suspension numerous settlement conferences were held between MPC and a majority of the intervenors. Six stipulations were submitted for PSC consideration in two sets of three. MPC is a party to all six stipulations. The intervenor parties to each of the six stipulations vary. Several of the intervenors did not participate in settlement conferences and several participated but chose not to stipulate. Most of the stipulations presented to the PSC are contested by one or more of the intervenors in this proceeding. Several issues in this proceeding were not directly addressed by the filed stipulations.

8. For each set of stipulations the PSC requested written comments from the parties on whether each of the individual stipulations should be approved as just and reasonable settlements of the issues or rejected in favor of further contested case proceedings. For this same purpose stipulation presentations before the PSC were conducted on both sets of stipulations. After the first stipulation presentation, the PSC approved Stipulation #1 and Stipulation #2 and deferred action on a third stipulation presented in the first set, the Gathering Stipulation. See, Notice of Commission Action (NCA) on Stipulations and Resuming Proceedings (April 17, 1997). The second stipulation presentation lead the PSC to approve the Bearpaw Stipulation and defer action on Stipulation #3 and the GTC-1 Stipulation. See, NCA on Stipulations (Second Set) and Resuming Proceedings (June 27, 1997). Action on the second set of stipulations was deferred in part because of compelling due process arguments made by several of the intervenors contesting the stipulations. Contested case proceedings were resumed by the PSC. A contested case hearing was held (beginning September 16, 1997) on the pending stipulations (deferred) and on all issues not stipulated to. Satellite hearings were held in Havre and Missoula. Arguments were submitted by the parties.

9. The PSC has fully considered the matter, the stipulations presented, the evidence taken at hearings, and the arguments of the parties supporting and opposing the stipulations. The PSC determines that the record in this case, applicable law, the public interest, and sound policy regarding the future of utility services, regulated and

unregulated, supports restructuring as stipulated to by the stipulating parties, but with certain qualifications and conditions set forth in the following discussions.

II. FINDINGS OF FACT AND ANALYSIS

A. STIPULATIONS

General

Preliminary Matters

10. The first set of stipulations (submitted to the PSC on or about March 12, 1997) includes: (a) Stipulation #1, on MPC's standard case (non restructuring) revenue requirement and a new compressed natural gas interruptible transportation (CNG-IT) rate; (b) Stipulation #2, on threshold, aggregation, pilot programs, transition period, provider of last resort, and customer information; and (c) the Gas Gathering Stipulation, on MPC rates for gathering services.

11. The PSC's April 17, 1997, NCA (referenced above) approving Stipulation #1 and Stipulation #2 and deferring action on the Gathering Stipulation also granted motions to resume contested case proceedings. Further settlement proceedings were conducted, paralleling the new procedural schedule. On May 9, 1997, MPC filed its "main case" rebuttal testimony which included, on behalf of itself and the stipulating intervenors, three new stipulations and testimony supporting the stipulations. MPC's rebuttal testimony also further addressed the Gathering Stipulation. MPC stated that it would abide by the Gathering Stipulation during the restructuring transition period even if the stipulation was not approved by the Commission.

12. The second set of stipulations includes: (a) Stipulation #3, on rate moratorium, allocated cost of service and rate design (ACOS/RD), competitive transition charges (CTCs) to recover stranded costs, supply contracts, and a uniform system benefits charge (USBC); (b) the GTC-1 Stipulation, on transportation general terms and conditions and on standards of conduct; and (c) the Bearpaw Stipulation, on firm receipt point capacity into MPC's South Bearpaw Line.

Relationship between Stipulations and Rules

13. The stipulations relate in part to matters upon which the PSC is, or likely will, address in rulemaking (e.g., standards of conduct, consumer protection, and uniform system benefits program). Rules, when completed, will be paramount to any tariff provsions resulting from this Final Order. Regarding PSC rules, one or more of the parties have suggested that PSC rulemaking can address certain expressed concerns in this case (e.g., standards of conduct). That might be true, but there is no certainty that the intended rulemaking will address those concerns. Therefore, issues pertinent both to the present case and possible future rules will not be deferred to rulemaking.

Burden of Proof / Support of Record

14. Several of the non-stipulating parties argue that MPC has failed to carry its evidentiary burden to demonstrate a substantial record through which the PSC may approve Stipulation #3 and the GTC-1 Stipulation. All stipulating parties argue that the stipulations are supported by the record. Whether the record's support would be sufficient to meet the burden an individual party might have as a proponent of a contested position is not certain. However, certainty on this point is inconsequential. In the stipulation or settlement environment strict "burden of proof" should not be a requirement or necessarily even relevant. So long as there is sufficient information "of record" such that the PSC can evaluate the agreed-to position, apply its expertise, make an educated determination in regard to all aspects necessary to fulfill its duties in rendering decisions, and act on bases capable of being clearly articulated, the record is sufficient. The PSC determines that there is legally sufficient support of record for the stipulations.

Stipulation #1, Stipulation #2, Gathering Stipulation, and Bearpaw Stipulation

Stipulation #1

15. The parties to Stipulation #1 (copy attached as Appendix 1) are MPC, DEQ, and MCC. They agree to a $0.935 million annual revenue requirement increase (excluding for restructuring). The original request from MPC was for $4.85 million. The stipulating parties agree to a rate of return of 11.25 percent. The agreement includes consideration of the Missoula Loop and the revenues associated with it as a post-test year addition. The results of the agreement are a non-gas cost increase of 1.27 percent. The stipulating parties also agree that this increase would be effective May 1, 1997, if the bond financing provisions of SB396 did not pass; otherwise it was to be effective after PSC final action on the restructuring case. The bonding provisions of SB396 passed. See sec. 69-3-1403, MCA.

16. These parties also agree that MPC will establish a new interruptible transportation rate (CNG-IT) available to a customer who has as a legitimate business purpose the dispensing of compressed natural gas (CNG) as fuel for motor vehicles. They agree that the rate shall include a monthly service charge (including meter charge) equivalent to that in MPC's D-ITG-1 rate and an interruptible commodity charge, being the product of actual monthly quantities and the maximum commodity rate in D-ITG-1 (unless otherwise negotiated between MPC and the customer).

17. The parties objecting to Stipulation #1 are PA and Ferdig. Both generally object to any stipulations which result in a piecemeal approach to regulation. PA specifically comments that granting a non-gas cost percentage to be effective prior to conclusion of the case partially takes away MPC's incentive to resolve the proceeding. Ferdig comments that MPC's recovery of the $0.935 million while the stranded cost issue is pending reduces MPC's incentive to resolve the stranded cost issue.

18. The PSC overruled these objections and approved Stipulation #1 (April 17, 1997, NCA). The PSC reaffirms that approval and adopts Stipulation #1 as an integral part of this Final Order, subject to qualifications and conditions as may be established by this Final Order. The stipulated annual revenue requirement is approximately $2.43 million less than requested by MPC in its filing. The stipulated rate of return, 11.25 percent, is the same as proposed by MPC in its filing and the same as

approved in PSC Docket No. D95.9.128 (MPC's last rate case pertaining to gas revenue requirements). As the bonding provision (of SB396) did pass, in accordance with the stipulation new rates will not become effective following this Final Order. That likely is some mitigation of PA's and Ferdig's concerns. Additionally, the PSC respects PA's and Ferdig's expressed disfavor of piecemeal processing of issues in matters before the PSC. However, the PSC disagrees that this case is being processed in such fashion. This case is not a collection of single issues being processed separately. This case is a multi-issue comprehensive case. Identifying and deciding individual issues within it is not piecemeal; it is the proper and accepted way of producing a decision in multi-issue cases, a decision which is of necessity the sum of the decisions on each of the issues.

Stipulation #2

19. The parties to Stipulation #2 (copy attached as Appendix 2) are MPC, MCC, GFG, LCG, DEQ, DOA, MHA, the Marketers, Enron, and NMOGA. These parties agree to lower the threshold level for transportation customers to 5,000 dekatherms (dkt) per year to allow customers the opportunity to choose their gas suppliers before the 1997/1998 heating season. In the original filing the Company proposed a threshold level of 10,000 dkt per year for the first three years of the transition period and 5,000 dkt per year for the following two years with no threshold after that. Stipulation #2 proposed the use of pooling for marketers to consolidate the requirement of eligible transportation customers under one transportation agreement. Pooling will be allowed in accordance with provisions within the new GTC-1 (discussed later). Single customers with separate meters on physically contiguous sites may aggregate loads.

20. A transition period for customers to move to choice was agreed to in Stipulation #2. The period is set not to exceed five years, ending on July 1, 2002. In accordance with the stipulation, six months prior to the end of the transition period, MPC will file a plan with the Commission proposing a method of assigning customers

who have not chosen gas suppliers. The Commission will then have the opportunity to decide whether MPC's distribution entity should continue its merchant function of providing supply for small commercial and residential customers based on the development of competition for these customers. MPC will use "best efforts" to develop a core aggregation for the 1997-1998 heating season (no longer a realistic expectation given the date of this Final Order). The stipulation agrees that MPC will conduct a core aggregation program (up to .5 bcf of MPC's annual load) no later than the 1998-1999 heating season. In accordance with the stipulation, a plan for such will be filed within 90 days of this Final Order.

21. The stipulation also addresses the issue of provider of last resort. In the instance of a customer not choosing a supplier, the stipulation requires MPC to provide bundled regulated sales service through the transition period. Certain guidelines are set out in the stipulation to give customers who do choose a supplier an opportunity to return to MPC's regulated sales service during the transition period. With regards to a supplier of last resort, if a customer's chosen supplier fails, the parties agree that the general terms and conditions (GTC-1) and contracts between shippers and MPC's transportation department will address this issue. Most of the risk will be placed on suppliers. The stipulation provides that MPC will retain the amount of storage resources needed to ensure system integrity and balancing. The amount of reserve needed and the GTC-1 were not agreed to in this stipulation (the GTC-1 Stipulation was filed later).

22. The parties expressing an objection to Stipulation #2 are PA and Ferdig. Their objections are similar to the ones made in regard to Stipulation #1. PA comments that settlement on reduction of the threshold takes away the intervening parties' incentives to resolve the proceeding sooner rather than later. Ferdig comments that the settlement of the threshold issue diminishes the incentive of larger customers to resist the imposition of stranded costs. The PSC overrules PA's and Ferdig's objections for the same reasons as stated in regard to Stipulation #1. The PSC doubts whether it has a valid role in providing incentives for any individual customer class to resist or not

resist on any issue; intervenors can and should determine for themselves the path they might want to take in furthering their interests.

23. The PSC has approved Stipulation #2 (as with Stipulation #1, see April 17, 1996, NCA). The PSC reaffirms that approval and adopts it as an integral part of this Final Order, subject to qualifications and conditions as may be established by this Final Order.

Gas Gathering Stipulation

24. The parties to the Gas Gathering Stipulation (copy attached as Appendix 3) are MPC, DEQ, and NMOGA. Through this stipulation these parties essentially agree to a permissible range of rates that MPC's supply division can charge for its gathering services, with several qualifications and exceptions for special circumstances. The parties supporting the stipulation seem to recognize that the PSC does not have authority over natural gas gathering, but suggest that when, as in the present case, a utility has gathering assets in rate base, authority over gathering can be reached as a condition to restructuring, particularly through any transition period that might result.

25. The parties expressing an objection to the Gas Gathering Stipulation are PA and Ferdig. PA comments that the stipulation, if approved, ensures that MPC's core and transportation customers will pay the stranded costs associated with providing natural gas producers with the "subsidized" gathering service. PA suggests that MPC should be required to charge actual costs for its gathering service. Ferdig's comments are similar and also specifically suggest that the maximum stipulated rate for gathering, $.40/mmbtu, is much lower that the actual cost, which could be as high as $1.75/mmbtu. Ferdig also suggests (April 11, 1997, stipulation presentation) that any PSC blessing on MPC's gathering proposal may constitute state action and remove MPC's gathering activities from antitrust oversight.

26. At the time it approved Stipulation #1 and Stipulation #2 (April 17, 1997) the PSC deferred action on the Gas Gathering Stipulation. The PSC now determines that it has no jurisdiction over natural gas gathering, it has not directly regulated

gathering even though gathering assets have been in utility rate base, and the PSC's ability to regulate gathering in some indirect way, if any, is further diminished through restructuring's removal of gathering assets from that rate base (a provision of Stipulation #3 and a requirement of sec. 69-3-1404(1)(a), MCA).

Bearpaw Stipulation

27. The parties to the Bearpaw Stipulation (copy attached as Appendix 4) are MPC, GFG, and Eagle Gas Marketing / John O. Brown (one of the Marketers). The stipulation addresses the firm receipt point capacity into MPC's South Bearpaw 8 and 10 inch pipeline (Bearpaw Pipeline) and provides that it will be made available up to the forecasted daily Great Falls load, not to exceed the physical capacity of the Bearpaw Pipeline in its present configuration (800 psgi). The firm receipt point capacity will change according to the Great Falls load and will be made available on a nondiscriminatory basis to all shippers. MPC's production capacity may be curtailed due to pressure increases related to the increased transportation volumes. The Company will accept nominations into the Bearpaw Pipeline up to the total forecasted daily Great Falls load. This agreement will be binding on any future owner, transferee or assignee of the Blaine County No. 3 interconnection or the Bearpaw Pipeline for not less than one year from the date of any sale, transfer, or assignment by MPC.

28. No objections were received regarding this stipulation. The PSC has determined that the Bearpaw Stipulation should be approved (see, June 27, 1997, NCA on second set of stipulations) and now reaffirms that approval and adopts the Bearpaw Stipulation as an integral part of this Final Order, subject to qualifications and conditions as may be established by this Final Order.

Stipulation #3 and the GTC-1 Stipulation

Stipulation #3

29. The parties to Stipulation #3 (copy attached as Appendix 5) are MPC, MCC, GFG, DEQ (a qualified agreement), LCG, and the Marketers. Stipulation #3

addresses several issues related to MPC's gas restructuring plan. It includes a rate moratorium on the new base rates, to be effective for a minimum of two years from the date of this Final Order. This does not include MPC's gas costs which will continue to be collected through gas trackers and the Gas Transportation Adjustment Clause (GTAC). It includes Competitive Transition Charges (CTC's) for stranded gas production assets (CTC-GP) and stranded gas regulatory assets (CTC-RA). The initial CTC-GP in the stipulation is $35.6 million. In its original filing, MPC proposed collecting a CTC-GP of $39 million. The $35.6 million could be decreased if there are any sales of the associated assets during the transition period. If Canadian-Montana Gas properties are sold during 1997 or the remaining transition period, proceeds in excess of book value prior to transfer will be shared, 20 percent to MPC and 80 percent to customers, as an offset to the CTC-GP. If Montana production properties are sold during this time, proceeds in excess of 25 percent of book value prior to transfer will be shared, 20 percent to MPC and 80 percent to customers as an offset to the CTC-GP. The stipulation provides that MCC and its representatives will have the right to review all contracts and agreements relating to the sale of gas production properties throughout the transition period.

30. The parties to Stipulation #3 agree to an annual restructuring revenue requirement to cover the CTC-GP at approximately $3.6 million for fifteen years. This annual amount is subject to change depending upon the actual interest rate and financing costs associated with transition bond financing. The CTC-GP will be paid by all core customers currently on MPC's system and customers who converted to transportation after September 1, 1993. Noncore customers that began transportation prior to September 1, 1993, and new customers connecting since November 1, 1991, not previously MPC customers, that have an annual usage of 60,000 mmbtu or greater will not be required to pay the CTC-GP. Also not responsible for the CTC-GP are customers with new annual loads of 5,000 dkt or greater who were not previously MPC customers and were connected to MPC's transmission or distribution facilities after December 31, 1996.

31. The CTC-RA proposed in the original filing was $32.7 million as opposed to $24.29 million agreed to in Stipulation #3. The amount to be recovered represents production-related regulatory assets and conservation investments. The annual restructuring revenue requirement to cover these costs will be $1.14 million for fifteen years. These costs will be recovered from all customers except Conoco, Cenex, and any new customers who were connected to MPC’s transmission or distribution system after December 31, 1996, with annual loads of 5,000 dkt or greater. In the stipulation, an allocation percentage is developed to show who will be paying the CTC-RA. Noncore customers who became transportation customers prior to September 1, 1993, will pay 24 percent, core customers, including those who converted to transportation after September 1, 1993, will pay 75 percent, and present utility customers will be responsible for 1 percent.

32. A purchase gas contract between MPC's supply division and services division is included in Stipulation #3. The contract is for the duration of the transition period and sets the rate and the amount of natural gas MPC's services division must purchase from its supply division. The volumes set in the contract are minimum amounts; the services division may purchase additional gas for core customers if there is demand in excess of the contract. Any additional purchases over the stated contract volumes will be sold to the services division for the lower of the market price or the contract price. The terms of the contract under the stipulation compared to the original filing are as follows:

	Stipulation Prices	Stipulation Volumes	Original Filing Prices	Original Filing Volumes
1st Year	$1.75/dkt	11.5 bcf	$1.586/dkt	14.0 bcf
2nd Year	$1.60/dkt	10.5 bcf	$1.586/dkt	12.3 bcf
3rd Year	$1.50/dkt	9.5 bcf	*	11.4 bcf

4th Year	$1.50/dkt	9.0 bcf	*	10.7 bcf
5th Year	lower of $1.60/dkt or market price	8.0 bcf	*	10.0 bcf
6th & 7th Years	NA	NA	*	9.3 & 8.8 bcf

* Redetermined on January 1 of each year; shall be the weighted average of Montana delivered gas price.

33. Stipulation # 3 also proposes a USBC to be assessed to all end-use customers. The $1.2 million that will be collected will be used for conservation and low-income discounts. The allocating percentage for the charge is as follows: noncore customers who became transportation customers prior to September 1, 1993, will pay 27 percent; and core customers, including those who converted to transportation after that date, will pay 73 percent.

34. MPC witness Cole, in his May 1997 rebuttal, asserts that Stipulation #3 settles allocated cost of service and rate design. Details follow on this stipulation's rate design content and on intervenor rate design concerns. For the duration of Stipulation #3's two-year (minimum) base rate moratorium these rates are fixed except for changes that arise due to gas trackers, the GTAC, and rebalancing due to MPC's discounting of transportation rates.

35. Stipulation #3 revises all customer charges. The residential tariff's customer charge rises to $5.25 from $4.62 per month and restructures meter (customer) charges to reflect cubic feet per hour flows on other tariffs. For the general natural gas service tariff (D-GSG) the restructured charges range from $12.50 per month to $75 per month, up from the current $10.98 per month customer charge rate. The transportation tariffs feature restructured customer charges that range from $175

per month to $325 per month. The firm utility gas contract tariff features a $100 customer charge.

36. MHA's witness Swinney filed surrebuttal on rate design. Swinney expressed doubt whether MPC's proposed meter charges (customer charges) reflect the cost to install and maintain meters. His concern was later rebutted by MPC's witness Maxwell (May 1997), who stated "the reality is simply that the total cost of a meter increases as the capacity of the meter does ... loads requiring large instantaneous flows of gas will require more costly meters and customers will be required to pay the resulting higher monthly meter charge." To Maxwell these charges are clearly cost based.

37. Because of the relation between Stipulation #2 and Stipulation #3, fixing the above customer charges implicitly resolves all rate design issues for the residential and general service tariffs. The Commission approves of the above customer charges and their implicit impacts on the balance of the residential and general service tariffs' rate designs.

38. Stipulation #3 changes the firm transmission tariff (T-FTG). The changes to the firm transmission tariff include a $6.00 per dkt capacity reservation rate and a maximum $.055 per dkt commodity rate. Enron's witness Walsh testified that changes to the firm transmission tariff are geared to larger (than 5,000 dkt per year) users, concluding that MPC's allocation of "fixed costs" to smaller transportation customers discourages such customers from pursuing transport service and therefore is an entry barrier. Walsh also testified that there is no evidence these charges exceed, or fall below, their cost of service.

39. While the Commission approves Stipulation #3 and, as a result, the firm transmission tariff rates, it finds necessary some further comments on cost of service. The Commission shares the cost-of-service concerns of some of the intervenors. A careful reading of Stipulation #3 reveals that it does not endorse or approve any cost theory, method, or party's view on cost of service. A similar outcome resulted from MPC's previous Docket No. 90.1.1. While stipulations may serve as an acceptable

expedient to resolve contested pricing issues, the resulting rate designs and rates should not drift far afield from their verifiable cost basis. Monopoly transmission, storage, and distribution services should be soundly based in incremental costs. Therefore, after the rate moratorium expires and if MPC seeks to recover additional revenues, the Commission requires MPC to simultaneously file an allocated cost-of-service study. The Commission and intervenors will then have an opportunity to revisit allocated cost of service issues for MPC's monopoly transmission, storage and distribution, and the potentially competitive supply function.

40. Stipulation #3 features flexible pricing for the firm transport of gas over MPC's transmission (T-FTG) system and over MPC's distribution (D-FTG) system. If the necessary and sufficient conditions are met, these tariffs allow MPC to discount ceiling prices down to floor price levels. If unutilized capacity on the facilities used to serve a customer exists (the necessary condition), MPC may discount ceiling prices to avoid uneconomic bypass or to increase loads (the sufficient conditions). If flexibly priced transmission and distribution rates are discounted, MPC may file to increase other rates during the two-year rate moratorium. Although approval of Stipulation #3 authorizes MPC to flexibly price (discount) firm transport tariff rates, the Commission is concerned with how MPC exercises this new authority.

41. First, it is not clear whether the ceiling prices MPC would discount exceed their cost of service. Even MPC witness Falvey states: “there is nothing wrong with lower rates for incremental use, so long as those rates cover full incremental costs.” Yet, MPC intends to discount those prices. The concern, therefore, is discounting in the presence of insufficient cost evidence. If an existing ceiling price for firm transport does not recover the full incremental costs, then discounting serves to exacerbate cross subsidies -- cost causers avoid their cost responsibility. Second, there is no evidence in this docket that excess capacity exists on MPC's transmission or distribution systems. Therefore, MPC has asymmetric knowledge vis-a-vis all other shippers as to the location of existing excess capacity on these two systems. Only MPC knows if the necessary and sufficient conditions have been met in order for a transport price to be

discounted. Even if all shippers were aware of those locations with excess capacity, MPC has not supplied cost evidence that would allow one to verify Falvey's concern that a discounted transportation price exceeds its incremental cost of service. Third, MPC may discount transport prices down to floor price levels. Evidence suggests that the floor prices may not be cost compensatory. While the evidence is shallow the Commission notes the concern so that a subsequent cost of service study will address the issue. Fourth, the Commission questions whether lost revenues due to price discounts are more appropriately defined and recovered as stranded costs. If defined as stranded costs, then the customers threatening bypass may not avoid the costs as they will with rate discounting. Fifth, with approval of Stipulation #3, and in turn price flexibility, MPC can paradoxically price higher quality firm service below interruptible service, an unusually inefficient outcome for a regulated service. When MPC files to recover lost revenues due to price discounting, the Commission will consider the appropriate source, and amount, of recovery.

42. Some further PSC observations might be appropriate on market power. First, if because of Stipulation #3 MPC's gas prices fall below market prices, then Enron's concern that the result stifles entry has some validity. However, it is only valid when residential and small commercial customers have choice, which at the earliest is not until the 1999/2000 heating season and could be as late as 2002. Consequently, there may be only a year when MPC could be advantaged. In any case, the Commission requires MPC to supply the Commission with market price data for comparison to the annual prices contained in the Stipulation #3. MPC should supply such information on a forecast basis for the markets surrounding MPC's Montana system. Second, MPC shall supply the Commission with quarterly reports on any price discounts tendered to its affiliate marketers.

43. As an additional point on market power, the Commission expects Stipulation #2's competitive analysis requirement to trigger a thorough market power analysis. The Commission may initiate a public process in advance of the required competitive analysis to establish relevant parameters and to collect relevant data.

44. Objections to Stipulation #3's stranded cost recovery (CTCs) are apparently not directed at the theory that restructuring utilities might be entitled to recovery of stranded costs, but to the costs that can be viewed as "stranded," at what value, and at what time they become recoverable. Section 69-3-1402(9), MCA, provides that transition costs include a natural gas utility's net, verifiable production-related and gathering-related costs, including costs of capital, that become unrecoverable as a result of customer choice and open access. Section 69-3-1402(6), MCA, defines "open access" as existing when a natural gas utility has made its facilities available to all suppliers, providers, and customers. Section 69-3-1403(2), MCA, provides, if a customer choice offering results in transition costs, the commission may allow those transition costs to be recovered in separate identifiable charges to customers. Enron argues that Stipulation #3's stranded costs are not verifiable. To Enron there has been no valuation of the so-called stranded costs. To Enron the costs must be independently verified and until that is done it cannot be established that they are recoverable. MHA argues in a similar fashion that MPC must demonstrate that the amount it proposes to recover has a basis in reality. To MHA the stipulated stranded costs have not been shown to be "net" or "verifiable." MPC argues that the controlling Montana statutes do not require a particular method of verification. MPC points out that the stipulating parties have used a cost of service basis for verification. The Marketers argue that the costs were verified through the stipulation process. MPC and MCC have both described in arguments Stipulation #3's cost-verification process. MCC's description is (MCC Post Hearing Brief (initial), p. 4):

> The record ... clearly supports a finding that MPC is faced with out of market costs related to its gas production and gathering assets. These above market, or uneconomic, costs are presently being recovered by MPC in rates charged for core market sales service. (Tr. ref. omitted.)
>
> The parties to [Stipulation #3] agreed to a total production related stranded cost value of $35.6 million, which equates to a production cost around $1.80/mcf. (Tr. ref. omitted.) As noted above, market prices appear to be somewhat lower. Therefore, the record supports the stranded cost value contained in [Stipulation #3].

45. The PSC determines the relevant legal requirement for "... net, verifiable ..." in sec. 69-3-1402(9)(a), MCA, must be interpreted in context familiar to utility regulation. It could be reasonably expected that different analyses would support different "net" "verifications." If there is at least one reasonable analysis pertaining to valuation of record and no others of record superior to it, the costs can be deemed "... net, verifiable ..." on that basis.

46. PA, Ferdig, and possibly other non-stipulating parties, also object to MPC's asserted stranded costs from a prudency standpoint. These parties argue that the PSC can and should do a prudency review of MPC's gas production activities to determine if related assets were prudently incurred and prudently retained or used and useful under the circumstances existing during the past ten (or more) years. These parties argue that the PSC has authority to do a prudency review. The PSC agrees that it has prudency review authority, used and useful review authority, and other powers. However, the legal question is not whether such authority exists, but whether there is a valid basis to do such review. No compelling reason has been provided by the objecting non-stipulating parties that the PSC must conduct a retroactive prudency review.

47. In this regard all involved admit that MPC's production assets are out of market. MPC offered the following explanation. MPC has acted reasonably and prudently. At all times the PSC was kept apprised. The PSC has continued to allow recovery for investments. MPC continued to act in a reasonable and prudent manner in 1987, the time at which Canadian border price dropped. MPC has retained its assets as a hedge in case the "gas bubble" would burst. Since that time, as recently as Docket No. 90.1.1, MPC has expressed related concerns and obtained PSC approval addressing them. MPC's ongoing investments in these assets were made to protect and improve operations for the benefit of customers. Utility taxation and depreciation requirements increase costs for utilities when compared to independent producers. MPC has been ordered by the PSC to make investments. MPC has acted with the best

interests of ratepayers in mind and in the belief that the PSC and the MCC endorsed its actions.

48. Ferdig's witness Jansky filed comments opposing Stipulation #3. Jansky contends that there is no record to support MPC's claim of more than $30 million in stranded costs. He does not believe that a record exists to show that the stranded cost determination meets the requirements of SB 396, which provides that stranded costs are based on costs that become unrecoverable as a result of customer choice and open access. Jansky states that if the allegations are true, these costs are not a result of customer choice or open access. Jansky also points out that, as required under SB 396, the costs must be net, verifiable production- and gathering-related costs. To Jansky, if the Company will not allow for an independent appraisal of its gas supply, an accurate determination cannot be made.

49. Ferdig believes that MPC has ignored claims that it has inflated the basis of its oil and gas assets by investing in them even after it was realized there would be rate consequences to ratepayers. Ferdig also believes that MPC has known since 1987 that it was cheaper to buy Canadian gas, but has misled the Commission as to the cost of Canadian gas and Montana gas. Ferdig's view is that MPC knew or should have known that information provided to the PSC was misleading and it was these misleading statements that prompted the Commission to make decisions that would enable MPC to overcharge its customers by approximately $100 million from 1987 through 1995 and thus MPC owes the ratepayers money. Jansky expressed Ferdig's position that these "prudent investment" questions are not out of the Commission's control even though they have already been incorporated into rates, as there have been cases regarding the prudence of investments years later based upon what the utility knew when the investment decisions were made. Ferdig believes that MPC misled the Commission and a prudency investigation is warranted.

50. Ferdig also believes that there is no evidence to demonstrate that money paid by parties who assumed gas supply contracts as part of Docket No. 90.1.1 for MPC gas supply contracts would cover the parties' share of stranded costs. It believes

stranded costs should be collected from all customers and any subsidies should be paid for by shareholders.

51. The Commission appreciates the time and effort spent by Ferdig in this case. It requires much fortitude for a relatively small entity operating in the backyard of the largest purchaser in Montana to carry on with an aggressive position contrary to the best interests of its largest customer. Looking back, it does appear that, in the late 1980's, MPC might have better foreseen the future of natural gas prices. Also in hind sight, it would have been desirable to have had more robust participation about the reasonableness of MPC’s gas costs in Commission rate cases during the 1985-1997 period, including an advocacy like that of Ferdig in this case. Such a viewpoint could have been presented in the late 1980's case in which MPC proposed, and then withdrew, its proposal to sell its gas properties at book value. However, in the final analysis, it was the Commission that declared MPC gas costs to be used and useful during this period. It did so based on the records in those cases and prevailing thoughts and views of the day. While this Commission does not intend to offer more reasoning in this Final Order than did the several Commissions that approved the gas costs in their orders, a brief explanation of rate making may help to clarify why Commission will not, in the present case, retroactively adjust gas costs for the period in question.

52. Rate making in Montana is prospective, and unless specifically directed otherwise by statute, the Commission sets rates based on property and operating expenses that are used and useful to ratepayers. Used and usefulness of expenses is an extension of used and usefulness of property, because, without the tools to provide utility service, there can be no expenses in providing it. Used and usefulness for each item of property and the underlying expenses may be considered either on a life cycle or a rate case-by-rate case basis. On a life cycle basis, properties are considered for addition to rate base after the properties are placed in service (used), application by the utility, and a demonstration that the properties are needed (useful). Upon acceptance by the Commission, these properties are depreciated over time and their rate base

values are not normally reconsidered in future cases. On a rate case case-by-case basis, each property in rate base would be reconsidered in every rate case until the properties were retired. With this approach, the utility would be continuously at risk for the difference between the market and book values of the properties, implying a higher cost of capital and, thus, higher rates to customers. Implicitly, the Commission has considered used and usefulness on a life cycle basis. Customers have shouldered the various risks over a property's life cycle in exchange for lower rates. If the Commission were to exclude the excess book value (over the market value) of MPC’s gas production properties from its pre-restructuring rate base, it would have essentially shifted the risk of market variance back to the utility without compensating it for that risk through a higher cost of capital. A corollary is if a gain of market value over book value were given to shareholders, a cost of capital reduction would be required. From a utility or a ratepayer perspective, this may not make good economic sense if the utility’s forecasts, upon which the original life cycle costs were based, are within a range of reasonableness, although disallowances may be be made if significant differences are found between these forecasts and actual test year operating expenses and asset performance. This proceeding is somewhat different from the traditional approach to rate making because of the legislative mandates of SB396. Essentially, the life cycle logic has been modified by society’s determination that the benefits of moving as quickly as possible to robust competition outweigh the benefits of vertically integrated monopoly. Therefore, the Commission finds no convincing evidence and argument in this proceeding to exclude as not used and useful any of MPC's gas producing properties previously admitted to rate base or the associated current operating expenses.

53 Enron argues that, under applicable statutory provisions, MPC's attempt to recover stranded costs is premature, and as a matter of law the PSC cannot approve recovery of them at this time. Enron believes MPC does not have statutorily defined "open access" and will not until all customers have choice. Enron further states MPC is requesting recovery of costs they predict will be stranded (unrecoverable) if the MPC

system ever gets to the point of full customer choice. Enron's argument is that open access and customer choice come first and only then are stranded costs valued and recoverable. MHA agrees that the costs must be caused by customer choice and not be merely a speculative award prior to implementation of choice. MHA contends the customer choice being proposed for implementation in this proceeding is to customers with at least 5,000 dkt annual consumption and that partial choice does not result in stranded costs. On these points MPC argues that it has opened its system, is further opening its system, additional customers will have choice now, and choice for others will follow through the transition period. MPC points out that Montana gas utility restructuring laws contemplate that not all customers will have choice at the same time, as demonstrated by sec. 69-3-1404(3), MCA,'s allowance for PSC jurisdiction over supply for customers who do not have or have not made choice. Along those same lines, MPC postulates that “become recoverable” in the phrase "[costs] that become recoverable as a result of [open access]", sec. 69-3-1402(9)(a), MCA, means costs that will become unrecoverable at some future time, but are identifiable today. MPC also argues that the statutory requirement for functional unbundling, sec. 69-3-1404(1)(a), MCA, requires removal of assets from rate base and creates stranded costs at the time of removal. The PSC agrees with MPC's assessment.

54 Enron objects to each revenue requirement part of Stipulation #3. First, regarding the 2-year rate moratorium, Enron supports the idea of enacting customer choice for customers through the core aggregation pilot program, but feels that the rate moratorium will negatively effect the ability to develop a viable core aggregation transportation program. Enron believes the rate design for small commercial and residential customers, under Stipulation #3, will discourage these customers from converting to transportation. Enron believes the average rate per dkt as a sales customer would be lower than the average they would pay as a transportation customer. Second, considering the CTC-GP, Enron feels that stranded cost estimates are not substantiated and would like to have the value determined through a competitive bid process. Without this process, Enron believes ratepayers are not guaranteed that they received the maximum compensation for properties. Enron also states that it is too early in the process to determine what costs are stranded. Enron argues that MPC has also failed to demonstrate that transition costs are not actually uneconomic production costs that were uneconomic prior to transition. Enron's feels that if the properties are transferred at less than their true market value, the MPC supply division is provided with an economic advantage over suppliers who are serving at actual market prices. Enron is opposed to any exemption given to any customer or customer class from paying for the stranded costs. Finally, with respect to the purchase gas contract (the five year purchase gas contract allows the MPC supply division to be the sole provider for the MPC services division, allows the services division to sell gas volumes that were purchased in excess of its needs and keep the difference, and allows the supply division to sell any gas that the services division does not purchase, directly to the market), Enron believes that the services division should be required to go to bid for its gas supply. This would require the supply division to enter the competitive market without any guaranteed support from the regulated operations. Enron believes that this tie between the divisions will make it difficult for customers to make a distinction between the two divisions.

55 Several of Enron's concerns have been addressed in discussion of the concerns of other parties. The Commission shares Enron’s concern that the most desirable outcome for customer choice would be for all customers immediately to be given the ability to choose among gas suppliers. However, a pragmatic view suggests that the present form of MPC’s vertically integrated natural gas monopoly has existed for public and private good since about 1930, and in this context, the five year transition period to competition is reasonable. The rate moratorium, which will become effective after the significant rate decrease from this case, offers core customers an immediate benefit while they are "quarantined" from choice during the transition period. Although not perfect, the Commission finds the rate moratorium in this context to be reasonable. As implied above, MPC must endeavor mightily to avoid exercising any and all abusive market power, including the appearance of such. In turn, the Commission intends to enforce the GTC-1 Stipulation's standards of conduct and to implement meaningful rules pursuant to SB396. Enron is right in asserting that without these protections, the transition and moratorium will not lead to meaningful, robust competition.

56 Enron also argues that costs, at least on a proportionate basis, do not become “stranded costs” until all customers have choice. The Commission has discussed this above and adds here that the problem is semantical. The plan for customer choice in Stipulation #3 includes all customers, although small customers will not be able directly to choose until the end of the transition period. Be that as it may, small customers, in addition to being beneficiaries during the transition period of MPC’s continuing obligations to provide traditional, firm and least cost utility service, are being given some of the advantages of cheaper gas supply in the transition period via supply/service division contract prices in years three, four, and five. While not perfect, this attribute, and the experimentation that continues during the transition period via pilot programs to best establish choice mechanisms, together demonstrate a “plan” commitment to choice that is sufficient to identify, quantify, and refinance stranded costs at cheaper interest rates and to include them in charges made to all customers.

57 MHA opposes the stipulations presented because it believes issues dealing with the restructuring of the natural gas industry should be decided by an evidentiary hearing by the Commission and not through the private negotiations of a group of industry specialists. MHA also believes that stranded cost amounts should not be based on a valuation submitted by MPC, but should be determined through an independent analysis. MHA's concerns may have some merit, but not sufficient to deny the settlement. For one thing, such action would very likely mean that medium size customers, such as some of MHA's members, would not have the opportunity to choose for at least another heating season a less costly source of gas supply. As MHA has pointed out, the loss of choice for one heating season may be more than offset if the Commission finds lower customer responsibility for stranded costs, presumably based on a valuation study that MPC or one of the intervenors would produce. However, the Commission may lack the legal authority to order MPC to conduct a valuation study of the type that the Commission or intervenors may prefer, and the Commission finds only sketchy evidence in this record of a valuation study conducted by an intervenor.

58 Other than the study of Canadian properties made by NMOGA witness Coolidge, which MPC rebuts, the real nub of the stranded cost concern in this case is MPC's Montana gas production properties. In response to questioning, MPC witness Callahan established two bases for stranded cost valuation of MPC owned reserves, which includes the Montana properties. Assuming that the sale of the Bearpaw reserves in Montana could be used for comparability to value all of MPC's reserves, a premise with which MPC disagrees, Callahan computed, in effect, a value for MPC stranded costs of about $7 million. On redirect, Callahan calculated the value of MPC reserves on a cash flow basis, which yields a stranded cost value of about $37 million. The stranded cost value in this case of about $35.5 million is clearly in the range of $7-$37 million.

59 Even if MHA and other like-minded intervenors in this case were to present a study which, in the final analysis, would reduce stranded costs to the mid

point between $7-$37 million, or $22 million, the effect on rates, particularly the rates of general service customers who become transportation customers, may not be less, at least for next two years, than rates which would result from Stipulation #3. The computations to make this comparison are complex; they involve a hypothetical reduction in stranded costs of $13 million offset by customer-contributed capital, the remainder of which is financed at the stranded cost bond rate projected to be 8 percent. For simplicity, one may use a ratio of 13/35.5 x $3.6 million. Over the fifteen year period of stranded costs recovery, the present value at 10 percent of this amount is $9.9 million. However, offsetting this amount would be the loss for at least one year of choice for customers at 5,000 mcf or more annual consumption, which very likely would have a value of several million dollars, the postponement of choice for an undetermined period for other customers, the loss for at least one year of the immediate rate reduction impact of Stipulation #3, which is about $3.7 million, and the loss for two years of MPC's error affecting GS customers that switch to Transportation, the present value of which at 10 percent would be $4.3 million. All told, when one factors in the risk to customers of continuing this proceeding in lieu of Stipulation #3, it appears to the Commission that Stipulation #3 offers a reasonable approach to resolving the stranded cost positions in this case.

60 NMOGA provided surrebuttal testimony through its witness Perry as its objections to Stipulation #3 and the GTC-1 Stipulation. In his testimony, Perry stated that shortcomings of the stipulations were with the contract price of natural gas, the gas contract, and MPC market power. The new contract price, according to Perry, includes the $12.2 million decrease in the CTC-GP that MPC originally proposed. NMOGA believes that the contract represents a subsidy to MPC's Canadian production and offers an alternative contract price structure. Perry's argument with the gas contract is that it gives MPC the power to unilaterally decide to displace Montana-produced gas with Canadian gas. Perry suggests that MPC has the ability to increase its sales volumes from Canadian gas and displace 20 percent of the Montana production. Perry also contends that MPC did not address the concerns about the effect on the property

tax values in Glacier County and lower taxes on wellhead rates. He also argues that gas purchase contract rights are not assignable even though the contract is, which doesn't make sense because the contract rights are what gives the property its value. Through Perry NMOGA asks that the Commission schedule supply volumes for Montana and Canada and require that contract rights be assignable. To NMOGA the contract adds value to the property and the 80 percent of the sales price over the transfer value could be used to reduce the CTC-GP and provide ratepayers with a secure supply of gas, and thus makes good business sense.

61 The Commission is partially sympathetic to NMOGA's views, but they, too, are not sufficient to overturn Stipulation #3. NMOGA's concern about whether some of the $12.2 million in stranded costs is included in the contractual gas cost of Stipulation #3 is valid, but only to a point, and only for the first year of the settlement. The supply/services division contractual gas cost differences between Stipulation #3 and the case originally filed has been discussed above. In the first year Stipulation #3 will cost customers about $1.9 million more than values in the originally filed case. However, contractual gas costs in years three, four, and possibly five very likely will be much less under Stipulation #3 than under the original case -- perhaps by $1 million or more. In any event, the stipulation offers core customers an element of protection in years three, four, and five not afforded by the original filing. The Commission finds that this protection in comparable gas costs is worth the first year increase of less than $1 million, after netting gas costs for years three, four, and five.

62 NMOGA is concerned about MPC Canadian gas, or other Canadian gas, displacing production from Montana. However, there is nothing in Stipulation #3 that preempts existing contractual provisions between the MPC supply division and third-party Montana producers. If an existing third-party contract contains legally valid and specific price and volume levels, the MPC supply division is contractually barred from dishonoring the commitment upon approval of Stipulation #3. If any of these contractual values are above market prices, they, too, constitute a form of stranded

costs, albeit one that most likely is less long lived than the costs of those properties directly owned by MPC's supply division.

63 NMOGA's concerns may ring most true when contract renegotiations occur, because MPC may use the lower cost of Canadian gas to pressure third-party Montana contractors to accept lower value contract terms. If true, over time the lower prices will benefit consumers, although, in turn, tax collections in Montana will be reduced. As a corporation over which the Commission has authority, MPC must be very cautious about advocating or causing dramatic, overnight changes to the taxing structures that have supported an important part of the societal infrastructure on which MPC has relied in conducting its natural gas business in north central Montana for so many decades. At the same time, the Commission is very aware that tax policy is in the purview of the Montana Legislature, and while, to some extent, it is controllable by that body, even it may be uncertain about revenues that may be raised because of the unforeseeable effects of changing economic and business conditions. The Commission and other entities are more on the edges of the issue than is the Legislature. Be that as it may be, the Commission commends to MPC the challenge of finding a win-win solution to lower customer gas prices and a smooth transition to a tax infrastructure that recognizes the advent of true competition. NMOGA’s suggestions of (a) bifurcating the supply/services contract into Canadian and Montana components and (b) contract assignment may solve just one half of the above challenge made to MPC. Additionally, although these suggestions offer NMOGA a degree of protection in the transition to competition, they do not allow MPC the flexibility it needs to manage its gas supply through the transition period to competition. Therefore, the Commission finds that these proposals alone are not sufficient to create the win-win solution envisioned by the Commission.

64 Objections to Stipulation #3 do not prevail. The PSC determines that Stipulation #3 should be approved and by adopts it as an integral part of this Final Order, subject to qualifications and conditions as may be established by this Final Order.

GTC-1 Stipulation

65 The parties to the GTC-1 (General Terms and Operating Conditions) Stipulation (copy attached as Appendix 6), on transportation general terms and conditions and standards of conduct, are MPC, GFG, LCG, DEQ, and the Marketers. Through stipulation these parties agree to proposed tariffs amending the current GTC tariffs through deletions and insertions.

66 The proposed tariff contains rules that govern operation of MPC’s transmission and distribution systems in an open access environment. MPC has had a GTC tariff since the conclusion of Docket No. 90.1.1. The existing GTC tariff should change to reflect experience and knowledge gained over the past five years. Whereas MPC’s direct June, 1996, testimony modified the GTC tariff, MPC’s May 1997 rebuttal changes the tariff to reflect the GTC-1 Stipulation. Among other requirements the GTC tariff includes balancing and standards of conduct provisions. These two provisions are the focus of the below findings.

67 To MPC, the GTC-1 tariff will protect customers from monopoly abuses and anti-competitive behavior. Pursuant to the tariff MPC's transmission department will follow the affiliate transaction guidelines of FERC Order 497, as proposed (with modifications) for incorporation into MPC's GTC-1, the supply division and MPC affiliates having access to transportation information only as made generally available to all shippers and producers.

68 MPC proposes that its distribution division not be required to enter into a contract for transmission (as other transmission customers are so required) because it will be acting on behalf of a large core customer load. There would otherwise be an administrative burden and a capital intensive nature for both the distribution and transmission divisions with no benefit for core or other customers.

69 MPC comments that supply transactions will be subject to regulatory oversight during the transition period. The price will be established in this proceeding for the first contract year and for following years it will be based on the average price

MPC pays to independent producers under delivered gas purchase contracts in Montana. MPC's distribution division will continue to make gas tracker filings during the transition period and purchases under the agreement will be monitored through those filings. Other sales by the supply division to make up the gas mix for core customers will be at market value and also monitored through the tracker filings. After the transition period MPC expects to have no merchant function but will compete for sales through its supply division.

70 MPC witness Griffin's May 1997 rebuttal lists changes to the GTC tariff that link the Company's direct testimony proposal to the GTC-1 Stipulation's version of this tariff. MPC witness Cole's May 1997 rebuttal testimony asserts the purpose of the GTC's standards of conduct is to ensure that access to the gas utility's transmission and distribution system is open and fair, and that the marketing affiliates of the utility will be treated the same as any third party marketer. Cole adds that MPC's and the FERC's standards of conduct differ.

71 In his August 1997 surrebuttal, Enron's witness Walsh testified on the GTC's balancing and standards of conduct provisions. Although he generally supports the revised GTC-1, he testified on and expressed concern with these provisions. His concerns with the GTC's balancing provisions involve the different monthly and daily balancing requirements. Walsh finds discriminatory MPC's ability to nominate between 80 percent and 125 percent of average daily base volume, whereas a marketer is penalized for negative daily imbalances in excess of 2 percent. Walsh does not articulate his monthly balancing concern.

72 Walsh strongly opposes the GTC's standards of conduct for not protecting against the transfer of customer information and employee knowledge between MPC's regulated and unregulated activities. His surrebuttal asserts that the sharing of employees and the transfer of knowledge via employees are an immeasurable benefit to MPC's unregulated division. Thus, Walsh believes the goal of promoting fair competition among all participants will not be achieved.

73 Walsh expanded on and then summarized his concerns at the September hearing. While encouraged by MPC's creation of a marketing affiliate to compete and conduct gas sales, Walsh continues to have concerns due to the incomplete separation of MPC's regulated operation and deregulated marketing affiliates. Walsh summarized his concern involving part K of the standards of conduct. Part K requires the utility and its marketing affiliates(s) to maintain separate books of accounts and records to ensure that separation is both functional and financial. There will be an allocation of costs associated with utility support personnel among the utility and its marketing affiliates. Utility support personnel includes any individual employed or retained by the utility who is not utility gas operating personnel, including administrative, supervisory and executive management, construction, engineering, accounting, legal, regulatory or financial personnel. The requirement will also ensure regulated ratepayers and other shippers do not subsidize the marketing affiliate's efforts. The utility will keep accurate records of cost allocations which will be subject to Commission review upon request. Walsh states that Enron strongly opposes that aspect of part K involving the allocation of costs associated with utility support personnel.

74 While approval of the GTC-1 Stipulation is in the public interest, the Commission continues to have lingering concerns, some of which Enron raised. One concern involves the apparent incompatibility between Stipulation #3 and the GTC-1 Stipulation. The apparent incompatibility between the GTC-1 Stipulation and Stipulation #3 stems from MPC testimony on how it intends to implement Stipulation #3's flexible pricing of firm transportation relative to the GTC-1's standards of conduct. The GTC's standards of conduct require the uniform application of MPC's tariff provisions to all shippers, including nonaffiliated shippers (sec. 20.3). Relevant parts of the GTC's standards of conduct include: (A) the utility shall apply a tariff provision relating to transportation in the same manner to the same or similarly situated affiliated and nonaffiliated shipper if there is discretion in the application of the provision; (B) the utility shall uniformly apply tariff provisions for all shippers; (C) the utility shall not, through a tariff provision or otherwise, give its marketing affiliates preference over

nonaffiliated shippers in any transportation and storage service. SB 396 requires Commission-approved standards of conduct to be in a tariff governing a utility's natural gas transmission, storage, and distribution services.

75 Since the GTC's standards of conduct mandate uniform tariff treatment of affiliates and nonaffiliates, a relevant question involves whether MPC intends to uniformly apply Stipulation #3's rate flexibility, discounting, authority uniformly to affiliates and nonaffiliates alike. From the following cross examination it appears MPC has no such intent.

76 MPC witness Orr was asked if MPC would willingly notify all marketers when it discounts its firm transmission and distribution (T-FTG and D-FTG) tariffs:

> Q. *... If MPC would actually begin discounting customers TFTG or DFTG rates, would MPC be willing to first notify all of the marketers, brokers for the purposes of competing for the customer's load ...?*
>
> A. *Those transportation rates are just for transportation. <u>No other marketers would be able to compete for that load under these rates</u>. We have the distribution system. We transport for those customers. If we discount that transportation rate, it doesn't impact our marketers. It's just a transmission transportation rate. It's not a gas cost rate, <u>so the marketers couldn't compete for that distribution level load</u>, anyway, to transport it.*

TR 73, September 16 p.m. (emphasis added).

77 MPC's witness Griffin was also asked whether MPC must and would notify other marketers of discounts offered to affiliates:

> Q. *There is no apparent bar to the discounting being applied to an MPC affiliate?*
> A. *None that I'm aware of.*
> Q. *If MPC were to discount to an affiliate, would you be required by any terms within the GTC-1 standards of conduct to <u>notify other marketers</u>?*
> A. *I need to go back and take a look at the standards and see if there is any specific requirement, but <u>none that I'm aware of.</u>*

TR 129, September 18, a.m. (emphasis added).

78 While the GTC appears to disallow MPC’s interpretation of how it can implement price discounts, the GTC falls short of explicitly requiring MPC to notify all marketers contemporaneously as required by FERC Order 497. As MPC witness Cole asserts the FERC’s and MPC’s standards of conduct do indeed differ. If MPC appears to use the GTC’s standards of conduct in a discriminatory manner, a market participant (shipper or customer) can lodge a complaint with the Commission. As SB 396 does not prohibit the Commission from making rules that delimit when and how a utility discounts prices, that avenue remains open to ensure uniform treatment of affiliates and nonaffiliates.

79 Enron expressed concern with how MPC’s services division is competitively advantaged by different balancing requirements and penalties than are imposed on nonaffiliate shippers. The Commission finds that the record is not entirely clear on the issue of balancing. There are at least two different situations for which one can compare balancing requirements. One comparison involves MPC’s regulated services division relative to unregulated nonaffiliates. This comparison appears the source of Walsh’s concern. In response to Walsh’s surrebuttal, MPC witness Smith holds that Walsh has made an inappropriate comparison. Enron has not provided any counterpoint that would cause the Commission to disapprove the GTC-1 Stipulation.

80 The Commission finds that MPC must eventually explain any and all differential balancing policies that remain after core customers are given the option of choose alternative gas suppliers. As noted elsewhere in this Final Order, once the two-year rate moratorium expires and MPC exercises its right to file a general rate case, the Commission intends to revisit the GTC-1's tariff provisions. If MPC seeks to correct an alleged $2 to $3 million dollar rate design error at its earliest opportunity, a general rate case could be filed in the fall of 1999. Not until the 1999/2000 winter heating season can marketers begin to compete for part of MPC’s core residential and small commercial customer loads. Since, however, all residential and small commercial customers will not have that option before 2001 and maybe 2002, there appears ample

time to make the transition and revisit the differing balancing rights for MPC services division and nonaffiliates. Therefore, in the long run, Enron's balancing concerns should not be a competitive advantage in the MPC services division's favor.

81 Enron's last GTC-1 tariff concern involves the need to completely separate MPC's regulated services division and nonregulated marketing affiliate activities. This separation issue is also a concern to the Commission. There may be no transparent evidence of abuse involving regulated and deregulated activities, yet abuse may exist but be difficult if not impossible to detect. Therefore, the Commission questions whether anything less than complete divestiture can ensure against affiliate abuse in the long term. Until such time as the Commission has a better restructuring model that clearly details a more complete separation, the current functional separation combined with the GTC-1's standards of conduct must suffice. Again, the Commission fully expects that two years from now an opportunity will emerge to improve upon this stipulation's results.

82 The Commission finds appropriate a finding on the need for a competitive market analysis proceeding. Although imposed by the Stipulation #2, likely not by SB 396, the Commission expects to initiate a proceeding that investigates the competitive nature of MPC's gas markets. If that proceeding is to yield information on a timely basis, the Commission may need to initiate the public process by mid year 2001. In the initial proceeding the Commission shall entertain analyses on the existence of competitive gas markets for residential and small commercial customers. Until such time as that proceeding is initiated, the Commission requests reports from MPC that track gas prices in regional markets. MPC must also report quarterly on the Montana retail and wholesale customers to whom MPC's marketing affiliates sell gas. This quarterly report may be proprietary, but must contain gas sales and prices and the discounted firm and interruptible transport rates MPC assessed for service over its distribution and transmission systems.

83 Enron believes the GTC-1 regarding the standards of conduct will not protect or prevent the transfer of customer information between the supply and services

divisions. Enron believes that the standards of conduct will not provide for equal treatment of affiliates and third parties or promote fair competition for all suppliers. Enron believes that opportunities for abuse can be eliminated if there is a complete separation of the marketing affiliate from the local distribution company (LDC) and by imposing standards of conduct that are more strict than the ones supported by MPC in the GTC-1.

84 The Commission is sympathetic to Enron's concerns and logic as it pertains to complete separation of the marketing affiliate, although approval of Stipulation #3 will not allow other actions at this time. However, if MPC demonstrates any abusive market power activities, the lay of the land underpinning Stipulation #3 will have changed. In these circumstances, the Commission may investigate such activities or process any formal complaints filed with it.

85 Enron argues that the functional separation required by sec. 69-3-1404(1)(a), MCA, is not being met through the stipulations because the gas contract functionally links MPC the services provider with MPC the supplier. The PSC disagrees that the contract provides a functional link within the statutory use of the term "functional." Furthermore, although Enron might not go quite so far, if Enron is arguing for some form of PSC-ordered divestiture, it cannot be legally done. Montana statutes only require functional unbundling. Section 69-3-1403(1)(a), MCA.

86 NMOGA proposes that there be substantial penalties for utility breaches of standards of conduct and other requirements related to fair dealings. NMOGA suggests that penalties would provide for a deterrent to violating the standard and also to grant a way to bar marketers who violate rules from selling in Montana. The PSC has weak fine authority by statute. The authority involves relatively small fines and a cumbersome process, including court action, for collection. It has long been the desire of the Commission to have clear statutory authority to levy fines and penalties at the administrative level. Without legislation permitting it, the PSC cannot expand on this authority.

87 NMOGA has concerns regarding MPC's market power in four major areas: customer information, customer education, market share, and penalties for non-compliance. Customer information should be shared freely which means sharing any information generated in obtaining utility service including call center records of the nature and scope of trouble calls, calls for energy audits and evaluations and requests for service that the utility could or could not provide. This sharing of information would eliminate the need for regulatory oversight of utility transactions in this area. Not providing customer names and numbers would provide for customer confidentiality.

88 NMOGA supports the idea of the Commission overseeing or administering customer education because MPC can not be expected to present a balanced picture. NMOGA witness Perry displays instances that he feels violate the standards of conduct in the GTC-1 Stipulation and presents these examples as illustrations of MPC's lack of unbiased information given to customers. In this regard the PSC retains general statutory authority to monitor and regulate MPC and will exercise that authority when and if it becomes necessary.

89 According to NMOGA, MPC has the ability to create barriers to entry because of the recovery of stranded costs. The money that the Company will receive for the stranded costs could be used to increase advertising or to engage in predatory pricing. If this occurs, NMOGA believes true competition will not develop.

90 NMOGA feels that if Stipulation #3 and the GTC-1 Stipulation are approved MPC will have no incentive to work with other parties during the rulemaking procedure and smaller parties will receive little consideration. NMOGA asks the Commission to accept the stipulations with the changes suggested by it or throw out the stipulations and proceed with a contested case.

91 The Commission agrees with NMOGA's market power concerns. The Commission will have weak fining authority until legislation changes that, but the Commission is confident that the standards of conduct as agreed to in the GTC-1 Stipulation and being developed in the current SB396 PSC rulemaking, will adequately

address the market power concerns. The Commission encourages all parties to participate in its rulemaking.

92 The PSC determines that the GTC-1 Stipulation should be approved and adopts it as an integral part of this Final Order, subject to qualifications and conditions as may be established by this Final Order.

B. ISSUES NOT STIPULATED TO

Special Service Charges in General

93 MPC witness Orr's May 1997 rebuttal testimony proposes to unbundle and establish special electric and gas service charges. These gas and electric charges include: (1) late payment, (2) returned check, (3) reconnection, and (4) engineering charges. As a general matter, the Commission disapproves the electric special service charges, in part, due to the insufficient noticing of the proposals in this proceeding. Procedurally, the Commission's notice excluded any reference to these electric charges. Electric rates ought to be discussed and resolved in an electric and not a gas docket. MPC may file to unbundle these electric special service charges in a special filing. Regardless of how and when MPC refiles, the Commission's concern with the lack of cost evidence for these gas charges applies with equal force to the electric charges.

94 The Commission is not entirely comfortable approving the other special gas service charges. This stems from an absence of reliable cost support and the possible double collection of revenues. Cost support is painfully lacking in this docket and specifically missing from the support for these charges. The double collection of revenues is a concern that rivals the absence of adequate cost information.

95 The Commission illustrates the double collection of revenues by way of MPC's 1 percent late payment charge. MPC has customers who pay their bills late and is authorized to recover the associated costs through rates. Now MPC seeks to unbundle and recover the same costs from the cost causers. Since MPC did not propose to reduce its existing rates simultaneous with the implementation of an

unbundled special service charge for late payments, MPC will collect the associated cost twice -- once in existing rates and again in the newly unbundled charge. For this reason MPC will double collect revenues associated with its proposed unbundled special service charges. The double collection of revenues is not limited to newly unbundled rates but also includes the proposed tightened line extension policies.

96 This issue of double collection will not hold up approval of these gas special service charges. After Stipulation #3's minimum two-year rate moratorium expires and MPC files to recover revenues not permitted by the Stipulation #3, the Commission expects MPC to report the amount by which these charges have double collected the associated revenue requirements. Detailed discussion of each of these charges follow.

Late Payment Charge

97 MPC witness Orr’s July 1996 testimony proposes a 1 percent late payment charge for gas and electric service. The Commission approves the 1 percent charge (for gas service) and allows MPC to begin accruing interest sixty days after a bill is rendered. The proposal by MPC is not out of line with late payment charges assessed by other utilities. An inquiry into MPC’s cost of providing late payment services must await MPC’s next allocated cost of service filing.

Insufficient Funds

98 Orr’s July 1996 testimony also proposes a $15 returned check charge for insufficient funds. While not a cost basis, other utilities charge $10 for returned checks. Thus, and absent detailed costs for MPC’s gas system, the Commission approves a $10 charge. If a future cost study reveals different costs, the Commission may consider a different rate.

Reconnection Charges

99 Orr’s July 1996 testimony proposes a $50 per meter reconnection charge for customers disconnected due to nonpayment and a $75 per meter reconnection charge for customers who voluntarily disconnected. MPC's proposed $50 to restore gas service to a customer whose service was discontinued for nonpayment is three to four times higher than some of the other regulated utilities’ reconnection charges and could present an unaffordable barrier to the restoring of service for low-income and payment-troubled customers.

100 Absent any cost basis, and in light of other utility rates, the Commission finds these reconnection charges excessive and rejects MPC’s proposed charges. Montana-Dakota Utilities Co.’s apparent reconnection charges for nonpayment and voluntary disconnections are as low as $12 and $20 respectively. Pacific Power & Light Co. apparently charges $15 during office hours and $60 outside of office hours. Great Falls Gas Co. charges $15 but exempts customers who are eligible for assistance from the Low Income Energy Assistance Program (LIEAP) or from Energy Share.

101 Until such time as the Commission has better cost evidence, MPC is authorized to charge a $12 reconnection fee for nonpayment and a $20 fee for reconnection due to voluntary disconnection. The Commission accepts MPC’s proposal to exempt LIEAP customers from the former charge.

Engineering Charges

102 Through Orr MPC also proposes to assess an engineering charge of $45 per hour. As noted below, under the topic of line extension charges, there is an unexplained relationship between this proposed engineering charge and MPC’s newly proposed line extension charge. The Commission is concerned about the circumstances under which MPC applies the engineering charge. For example, it is unclear whether MPC will apply the charge as a preliminary assessment with each gas line extension inquiry. It is also unclear how MPC combines the charge with this docket’s newly approved line extension policy. Therefore, until such time as MPC

seeks to increase revenues once the Stipulation #3's minimum two-year time constraint expires, MPC may assess this charge.

Gas Line Extension Policy

103 MPC witness Maxwell's May 1997 rebuttal addresses line extension related issues. He proposes a $7 per dkt free extension allowance for residential, and a $5 per dkt allowance for commercial line extensions. Additionally, such customers shall receive in their free extension allowance a service line, regulator, and meter. MPC proposes an individual line extension analysis for transport customers. Because the transmission and distribution functions must stand alone without gas supply revenues and costs, MPC believes these policies should be revisited after the five-year transition period. Equity between new and existing customers will be the major consideration in that subsequent cost of service investigation.

104 In the same tariff on line extensions, MPC proposes other changes that reference Maxwell's July 1996 direct testimony. First, MPC proposes to charge customers a deposit for gas service. Second, MPC proposes another revision to clarify the intent of the word "minimum" in the line extension tariff (in the past customers have apparently interpreted the word to mean they can negotiate a larger than intended free extension allowance).

105 With reservation the Commission approves these gas line extension proposals. One concern involves the relation to MPC's special service engineering charge discussed earlier. MPC's testimony leaves unanswered how it intends to combine its new line extension policy and the engineering fee.

106 Another concern involves the potential double collection of revenues as a result of MPC tightening its free extension allowances. If, for example, MPC normally experiences about 3,900 residential gas line extensions per year and if a third of these 3,900 new customers took advantage of the $14 per mcf allowance, this docket's tightened line extension policy would shift about one million dollars in annual revenue requirements to new residential customers without lowering rates to existing customers.

As with the special service charges, there would occur a double collection of revenues given the new policy does not have a simultaneous and offsetting revenue requirement reduction. These are not minuscule rate impacts or trivial rate issues. The exact amount MPC double collects remains an empirical question.

107 MPC's double collection of revenues is a concern that gives the Commission pause. Gas supply, is potentially, but not yet, competitive. The provision of line extensions is a monopoly service that should continue to be regulated to mitigate any utility abuse that may arise due to its unique market power.

108 For the time being the Commission requires MPC to provide the following information. As a benchmark, MPC must describe gas line extensions by customer class for this docket's test year. That description shall include: (1) the number of extensions; (2) the average total MPC cost; (3) the average additional customer cost not covered by the then existing line extension policy; (4) the average number of hours spent and revenues collected on engineering each line extension; (5) the physical length and nature of extensions for both gas mains and stubs. These benchmark data must be provided within a year. In each subsequent year, MPC must then provide the above information for the new line extension policy.

Residual Rate Issues

109 At the September hearing MPC witness Orr was asked to comment on other tariffed rates not addressed by Stipulation #3. Orr conceded that Stipulation #3 does not address: (1) floor prices for flexibly priced firm and interruptible transmission and distribution transport tariffs (respectively T-FTG, T-ITG, D-FTG and D-ITG); (2) a balancing penalty on the firm transmission tariff (T-FTG); and (3) the balancing penalty and unauthorized system use rates on the interruptible transmission tariff (T-ITG). Although her testimony is at odds with Stipulation #3's content, Stipulation #3 also excludes any reference to firm storage rates (T-FSG).

110 With Stipulation #3's partial resolution of all rate issues, the Commission is left to decide rate levels for other rates on the above noted tariffs. As in Docket No.

90.1.1, this docket's stipulations do not approve of any particular costing theory, costing method or any party's views on costing. Consistent with the approval of stipulated rate levels the Commission approves rates in MPC's May rebuttal testimony that complement the stipulated rate levels.

Joint Residence and Nonresidence Gas Usage

111 Orr's May 1997 rebuttal proposes to modify the general natural gas service (GSG) tariff involving joint residence and business gas usage. That modification appears on the GSG tariff and reads as follows: "Where a portion of a residential dwelling unit is used for nonresidential purposes, General Service Schedule No. D-GSG-1, will apply to all service used for nonresidential purposes. If installation of a separate meter is impractical, Schedule No. D-GSG-1 will apply to all service rendered."

112 Because the criteria MPC may use to implement this new proposal are vague the Commission finds necessary the following modification to MPC's proposal. MPC must apply a predominate use criterion. With this criterion, the customer will be billed under the tariff which constitutes a majority of the customer's connected load.

Miscellaneous Amended Tariffs

113 On June 17, 1997, MPC proposed to amend two tariffs that were included in MPC witness Orr's May 1997 rebuttal. MPC first proposes to amend the USBC tariff to conform with language in Stipulation #3 -- whereas the low-income discount has been recovered from core distribution customers, it becomes part of the USBC for recovery from all end-use (non-utility) customer classes.

114 The second proposed amendment involves the firm storage tariff. Orr's proposal states that the firm storage tariff's sixth special term and condition has been changed to make the accounting procedure consistent with current practices. MPC asserts the amendment provides for shippers to pay applicable transportation charges when their gas is withdrawn from storage and delivered to the shippers' point(s) of

delivery. By continuing to operate under current accounting practices MPC adds that the amendment impacts shippers less and streamlines accounting for storage activity in conjunction with the new pooling provision. MPC asserts there are no financial impacts.

115 Given PSC approval of Stipulation #3, the USBC amendment is approved. MPC's gas storage amendment reverses the proposal in MPC's testimony. While MPC's reversal on how it proposes to bill for gas transportation remains puzzling, the Commission sees no reason of record, or otherwise, to reject it. Therefore it, too, is approved.

Interconnection

116 Interconnection, primarily in the vicinity of Billings, between MPC and MDU, is one of the two additional issues identified in this docket. Commission Order No. 5856d in MDU Docket No. 95.7.90 had deferred an issue involving this interconnection. In that MDU docket, DEQ had asserted an interconnection between MDU and MPC would mitigate load loss and enhance competition. MDU responded, in part, that DEQ had no idea of the cost of an interconnection or whether MPC had any firm capacity. The Commission deferred action on the issue until such time as an MPC docket could be used to explore the merits of the issue from MPC's perspective. Docket No. 96.2.22 provided the first opportunity for the Commission to investigate this issue from MPC's perspective.

117 Limited testimony was filed on this additional issue. MPC's witness Griffin (November 26, 1996) prefiled testimony to the effect that MPC would perform a net benefit analysis prior to making any interconnection investment. Customers may also contribute to an interconnection if the net benefit analysis did not justify an interconnection. Griffin added that MPC has about 16,000 dkt per day of noncommitted firm capacity that originates on the south end of MPC's system. No firm pipeline capacity exists between the north end of MPC's system and Billings. As for reciprocity in open access, Griffin adds that an interconnection would increase competition among gas suppliers by providing customers more choice. If the Commission ordered an

interconnection, he adds that the costs should be shared among the pipeline's customers.

118 This interconnection additional issue might be worth pursuing at a future time. This docket will not reach closure on the issue. Despite the competitive benefits MPC identifies and the valid point raised by DEQ in the previous docket the Commission will not require interconnections at this time.

Aggregation

119 Aggregation is the second additional issue identified in this docket. It arose in regard to MPC initial testimony. In his July 1996 testimony, MPC witness Cole referred to several pilot programs for customer aggregation but then deferred further discussion to MPC witness Corcoran. Corcoran described an experimental gas aggregation program for LIEAP and then deferred the discussion of other pooling programs to MPC witness Griffin. Instead of a comprehensive proposal to aggregate customer loads MPC proposed to initiate an informal process at the conclusion of this docket.

120 Rather than postpone load aggregation until this docket's conclusion, the Commission raised this as an additional issue. MPC was directed to design an aggregation program for the minimum number of average load residential and, or, commercial customers required to meet a 10,000 dkt per year threshold. The costs to aggregate customer loads were to be estimated and the necessary terms and conditions for a tariff were to be provided. At its own option MPC was invited to vary the base case assumptions and, in turn, provide additional cost and pricing information.

121 MPC witness Griffin prefiled testimony on this additional issue, proposing to lower the transportation threshold from 10,000 to 5,000 dkt per year. He referenced MPC's core aggregation pilot program and load profiling as a means to enable core customers to avoid economically infeasible meter charges. Customers with less than 5,000 dkt per year could then aggregate loads to meet this threshold. Other larger customers could pool loads.

122 Griffin's additional issue testimony also listed goals and objectives for a core aggregation program. MPC changed its initial filing to make supplier choice available to 500,000 dkt per year of core load beginning in the 1998/1998 heating season, made up of a minimum of 10,000 dkt per year of aggregated annual load of which at least 70 percent must be residential customers. The program offers aggregation on a first-come, first-served basis until the 500,000 dkt is attained. MPC outlined the following issues (condensed) that a core aggregation program must address: (1) supplier eligibility (licensing); (2) MPC administrative/operation issues (e.g, billing, opting in and out of the program, peak load forecasting responsibility); (3) gas supply issues (assignment of MPC gas supplies, storage, backup and provider of last resort); (4) core aggregation transport service (load profiling, balancing, penalties); (5) evaluation plan (allow stakeholder feedback on the pilot's success, surveys to monitor customer satisfaction); (6) Commission reporting (for Commission's information needs); and (7) communication plans (marketing and billing).

123 Stipulation #2 addresses, among other matters, issues involving load aggregation. It does not, however, explicitly address the Commission's additional issue on aggregation. With approval of Stipulation #2, MPC must conduct a pilot aggregation program no later than the 1998/1999 season. If the pilot program succeeds, MPC's remaining gas customers may move to gas transport "beginning over the next two heating seasons following the pilot." Thus, all residential and small general service customers may be able to choose a gas supplier by 2002. A complete core aggregation program must be presented to the Commission within ninety days of a Final Order in this docket.

124 For the time being, the Commission finds Stipulation #2 to adequately address the intent of the additional issue. The stipulation leaves unexplained what will happen if the pilot does not succeed or if the pilot continues for more than one heating season nor does it establish criteria on which to judge a pilot program's success. These and other detailed implementation issues should be addressed in the core aggregation plan MPC must file within ninety days of the date of this Final Order.

III. CONCLUSIONS OF LAW

125. All introductory statements, findings of fact, and analyses above which can properly be considered conclusions of law and which should be considered as such to preserve the integrity of this order are incorporated herein as conclusions of law.

126. MPC is a public utility. In accordance with Title 69, MCA, the PSC has jurisdiction over MPC as a public utility and over the matters and issues which MPC and the intervenors have presented in regard to this docket. This matter was properly noticed and heard in accordance with Title 69, Chapter 3, MCA, and Title 2, Chapter 4, MCA.

ORDER

1. All conclusions of law which can properly be considered an order and which should be considered as such to preserve the integrity of this order are incorporated herein as an order.

2. All pending objections, motions, and arguments not specifically having been ruled on in this Final Order (if any) shall be deemed denied, to the extent that such denial is consistent with this Order.

3. This Final Order is final PSC action on all gas-related issues arising from all dockets which have been consolidated into this matter (e.g., MPC's 1994 gas cost tracker Docket No. 94.11.50, MPC's 1995 gas cost tracker Docket No. D95.12.166, and MPC's 1995 general rate case Docket No. D95.9.128). Pending arguments pertaining to issues in those dockets and not specifically ruled on herein (if any) shall be deemed denied, to the extent that such denial is consistent with this Order.

4. The Montana Public Service Commission, being fully apprised of all premises, HEREBY ORDERS that MPC shall restructure in accordance with Stipulation #1, Stipulation #2, Stipulation #3, the GTC-1 Stipulation, and the Bearpaw Stipulation, as qualified and conditioned by the PSC in the above Introduction, Findings of Fact and Analysis, and Conclusions of Law. The Gathering Stipulation is not approved for the

reasons expressed above (i.e., PSC jurisdiction). MPC shall comply with this Final Order in regard to all issues not stipulated to, also as set forth above.

5. The Commission wants rate changes resulting from this docket to be concurrent with those in MPC's upcoming annual gas cost tracker, which MPC will file on or about November 1, 1997. To acheive one concurrent change in rates on or about November 15, 1997, or on such other date considered to be reasonable by the Commission after its review of the tracker filing, the Commission directs MPC to establish an accounting to keep track of the rate decrease from the date this Final Order is served until the date that rates are changed concurrently with those of the tracker. Interest on the account balance shall be computed on a compounded monthly basis at MPC's rate of return on gas equity. The final account balance shall be included for the Commission's consideration in MPC's 1998 gas tracker filing.

Done and dated this 28th day of October, 1997, by a vote of 4-1.

BY ORDER OF THE MONTANA PUBLIC SERVICE COMMISSION

DAVE FISHER, Chair

NANCY MCCAFFREE, Vice Chair
(WRITTEN DISSENT ATTACHED)

BOB ANDERSON, Commissioner
(OPINION ATTACHED)

DANNY OBERG, Commissioner
(CONCURRING OPINION ATTACHED)

BOB ROWE, Commissioner
(OPINION ATTACHED)

ATTEST:

Kathlene M. Anderson
Commission Secretary

(SEAL)

NOTE: Any party may request the PSC to reconsider this decision. A motion to reconsider must be filed within ten (10) days. See 38.2.4806, ARM.

(Appendix 1 through 6 not available electronically. Please e-mail tshorten@mt.gov to request a copy. Please provide name and mailing address.)

Dissenting Opinion of Commissioner McCaffree
MPC Natural Gas Docket 96.2.22, Order No. 5898d

The stranded cost portion of Commissioner Rowe's opinion, for this docket, is well thought out and well written. I cannot state it any better.

The Commission has little latitude as to when customer choice must begin. The information supplied by Montana Power Company during the stipulation presentation in September, did not leave a convincing record that the amount requested for stranded cost recovery is not excessive. The amount of money involved is not enormous; however, it is money the ratepayer is being asked to pay. Is this portion of the stipulation enough to stop the process of implementing competition for natural gas supply? I believe so. The record leaves enough of a question in my mind that I must, in good conscience, vote "no" to accepting the stipulation.

The order, written using the information we have on record, may be the best we can do to uphold the direction given us the 1997 legislature. The Public Service Commission staff did an excellent job of working through the stipulation and writing the order. The record they had to work from was simply not enough for me to cast an aye vote, which I feel certain is asking the ratepayer of Montana to pay more than their fair share of costs.

RESPECTFULLY SUBMITTED this 31st day of October, 1997.

Nancy McCaffree
Vice Chair

Opinion of Commissioner Bob Anderson
MPC Natural Gas Case 96.2.22

Regulation of the natural gas monopoly has served reasonably well. Prices have been fair and reasonable and service good. But irresistible forces of change are at play. These are the forces of global competition, technology, and customer choice. Conventional belief (shared by me) is that these forces will ultimately provide customers with lower prices and better, innovative service.

Congress first recognized these forces in 1978, thanks to the Arabs, when it began the deregulation of wellhead production.

The Federal Energy Regulatory Commission recognized these forces through the 1980s and 1990s (culminating with Order 636) when it separated the merchant and transportation functions and opened the interstate pipeline system to non-discriminatory access.

The Montana Power Company and the Public Service Commission recognized these forces in the 1990-91 gas transportation case (PSC Docket No. 90.1.1) which began unbundling the MPC system and offered customer choice to large customers.

The PSC recognized these forces in 1996 when it issued its request (Order No. 5898 in this present matter) to Montana Power Company to file a comprehensive case and further unbundle its system.

The legislature recognized these forces in 1997 when it adopted SB 396.

I believe we will look back on this order as the second of three major orders (the first was Order No. 5474c, out of PSC Docket No. 90.1.1; the third is yet to come) which will lead eventually to full competition in the production sector of the industry and customer choice for all, even the small, residential customers.

As with most things in life (especially at the PSC), this case had it procedural and substantive aspects.

The procedure was protracted, beginning with the issuance of the February, 1996, notice to MPC to file a comprehensive case. The procedural schedule was suspended many times to:
1. encourage the parties to seek settlements, and 2. allow the legislature act. The parties produced six settlements which resolved most issues. In the end, the contested case hearing involved whether or not to accept the settlements, specifically Stipulation #3 and the GTC-1 agreement (on general terms and conditions).

By definition, settlements are compromises. So, often, are the outcomes of fully litigated contested cases. It's tempting to dislike some aspects of the settlements we considered, but it's impossible to know if a better and quicker outcome would have resulted from contested case litigation.

This order has many positives:

> The minimum threshold for customer choice will be reduced from 60,000 to 5,000 dekatherms/year.
>
> Rates to residential customer will be reduced about 3.4%.
>
> Residential rates will be frozen for two years (tempered perhaps by tracker and financing filings).
>
> Supply costs for residential customers will decline over the next five years.
>
> Pilot programs will explore how to provide customer choice to small customers.
>
> A universal system benefits charge will fund conservation and low income programs.
>
> Ratepayers will capture a portion of MPC production assets sold in the future.

The order is not without its negatives:

> Core customers will pay stranded costs, on the order of $60 million. Although this amount may be reasonable, the record is opaque on whether or not it is justified.
>
> Core customers will be obligated to pay stranded costs, through a competitive transition charge, for 15 years.   That's too long in a rapidly evolving industry.

In addition, the case produced several lingering worries:

> Some parties asserted credibly that the competitive deck will be stacked in the Montana PowerCompany's favor because of inadequate control over the relationships between MPC's supply and service divisions and other potentially anticompetitive practices.
>
> Montana gas producers could be lose market share.
>
> Tax revenues in gas-producing counties could be reduced.

At the same time, there is hope:

All customers should have choice by 2002.

The PSC, through monitoring and rule making may be able to detect and cure anticompetitive practices.

In the next five years the third (and final?) step will be taken, bringing customer choice to all.

The PSC was faced with two choices: accepting the stipulations, with their warts, or rejecting them and returning to a full contested case. Our decision was aided by the vigorous and competent, (and in some cases courageous) participation of the many parties.

Given the downsides of the stipulation package, especially the stranded costs outcome of Stipulation #3 and the weaknesses of the GTC-1 stipulation with respect to potentially anticompetitive practices, it was tempting to reject these agreements, believing that the PSC could produce a product which better represented the public interest. However, that option had a fatal flaw: under the terms of SB 396, it is the option of the regulated utilities to file restructuring plans. I concluded an imperfect bird in the hand was better than a bird in flight.

RESPECTFULLY SUBMITTED this _____ day of October, 1997

____

Bob Anderson, Commissioner

Concurring Opinion of Commissioner Oberg
MPC Natural Gas - Docket 96.2.22, Order No. 5898d

Commission orders speak for themselves. I heartily agree with the findings of this order. Expanding customer choice for all natural gas customers is in the public interest. The terms and conditions presented in the stipulation and in this order represent a fair and reasoned approach to achieving that end for all Montana Power customers. While the order is sound, I find it somewhat austere for such a major switch in public policy. This order incorporates a historic change in the way Montanan's purchase natural gas services that deserves noting. To those involved in the utility industry and familiar with the trends nationally to end the traditional utility monopolistic business structure the order is reasonable. I am concerned the more casual observer may be left wanting further explanation for the orders conclusion. The answer to the larger question "Is further customer choice for MPC customers in the public interest?", seems so obvious to us that it appears to go unanswered in the order. In my opinion it begs to be answered. My intent in this separate opinion is to expand on those concerns, clarify where I might disagree with my colleagues and offer guidance on future regulatory responsibilities.

In ordering Montana Power to file a comprehensive rate case, including the issue of restructuring the natural gas business unit to allow for customer choice, the Commission recognized that such a move under the right conditions could be in the public interest. It was the Commission's intent to use the filing and the contested case process as a vehicle to determine the conditions under which restructuring would represent sound public policy. The Commission has generally believed it possessed sufficient authority to effect such a change. The 1997 Legislature furthered that cause when by a near unanimous vote it provided a loose policy framework in SB396 that added further credibility to the notion that ending the monopoly could represent a public benefit.

It is interesting to note that such a major paradigm shift in delivering utility services would find so little resistance. While there was some dissension in ***how*** such a change should occur, no party in this case took issue ***if*** the change should take place. The devil would prove to be in the details.

Even the devil appeared not to be Satan himself, for a majority of the intervenors were able to meet at the negotiating table and offer the PSC a series of stipulations that in total set the stage for an orderly transition to a competitive natural gas structure in the Montana Power Service territory. Given the lack of dissent over the merits of restructuring it became a non-issue, and the order rightly focuses on whether the stipulations represent a fair set of conditions to this new environment for the various stakeholders in the business- the company, the customer, natural gas suppliers, and new entrants - to name the primary players.

As such the Commission was faced with these issues:

---Does the stipulation represent good public policy?

---Does the stipulation pass the traditional regulatory test which is usually condensed as fair and reasonable rates and adequate service?

---Does the stipulation package conform to legislative direction as passed in SB 396?

---Given that both the Legislature and the Commission have determined that expanded customer choice could be in the public interest, do the terms and conditions of the stipulation further the broader public policy goals of developing an opportunity for robust competition to develop?

---While the majority of intervening parties either endorsed or offered no opinion on the stipulation, the Commission was confronted with dissenting parties who advocated rejection of the stipulation. Any governmental agency has an obligation to carefully protect the rights of those who advocate minority opinions. This responsibility is even greater in this instance due to discrepancies in economic power of the dissenters as compared to the applying utility, and as such, the PSC has a critical obligation to critically examine the dissenting parties position for merits.

---Would the interests of ratepayers be better advanced by a PSC directed decision rather than the settlement?

I concur with the technical analysis and findings in this order. Opponents of the stipulation were not persuasive that the package of stipulations were not a fair and reasonable path to full customer choice. Conversely, the varied and diverse parties who presented the stipulations to the Commission even though the Commission offered a procedural “out” for a full evidentiary hearing, provides powerful evidence for this Commissioner that the stipulations meet a strict test of good public policy. MCC witness, George Donkin, who has aggressively advocated aggressive consumer positions in past dockets unequivocally endorsed the stipulations in a statement to the Commission. His is a powerful voice for consumer interests that the Commission would have been remiss to ignore.

Donkin presented compelling arguments why the Commission should ratify the stipulation:

1) Small consumers will pay overall rates which are lower than what either the company originally proposed or is in current rates. The net effect of Stipulation #3 combined with prior agreement on non gas revenues should result in a residential rate decrease of 3.4%.
2) The 2 year rate freeze and the 5 year schedule on the price MPC can sell its own natural gas to MPC customers represents significant lasting concessions to small users. Customers are assured declining gas contract prices irregardless of the market for 5 years.
3) The stranded cost figure agreed to in the settlement is legitimate and within range of reasonableness and he acknowledged MPC has a right to expect recovery. The negotiated production related to stranded costs of $35.6 million is about 25% less than requested. The full amount of these production related and regulatory asset costs are currently included in rates
4) The stranded cost recovery mechanism does not act as an anti-competitive barrier.

I concur with the testimony of Mr. Donkin. The stipulation offers significant value in the present for even small customers. That value can only increase over the transition period as customers gain the ability to exercise customer choice.

It would do history a disservice to not record in this order broad public policy benefits offered by this stipulation. One must note that MPC has voluntarily agreed to open its system and traded the protection of the traditional utility compact of a reasonable rate of return for an uncertain economic future. While one must conclude they believe sound management and innovation will over time deliver significant shareholder benefits, one can not easily conclude by the record that such an outcome is probable. On the other hand, this Commission can fairly conclude from the preponderance of evidence and generally accepted economic theory that abandoning the monopoly structure can lead to significant ratepayer and societal benefits. The risks of the new environment may well be far greater on MPC than the possibility of adverse consequences on consumers. Given that MPC has voluntarily accepted this measure of risk, the Commission's greatest concern has to be on weighing adverse impacts on ratepayers. Competition can generally be expected to result in lower rates (or at least lower than in a regulated environment), product and service innovations, and other intangible benefits of competitive forces. That conclusion seems uncontested in this docket.   To deny consumers these benefits or even delay them would require a strong showing that opponents had found a fatal flaw in the stipulations. Any shortcomings shown by Ferdig and others in this docket are far from mortal wounds.

I believe at best the opponents outlined potential weaknesses in the plan, but failed to offer conclusive evidence that would justify this Commission rejecting the stipulations. Many of the parties concerns about level playing fields, potential for affiliate abuse, and tax consequences can be addressed in subsequent rulemakings or other forums like the Legislature.

Stranded costs were the most controversial issue in this case, which is not surprising as that is where the money is.   I am skeptical enough after 15 years as a regulator to believe that parties who argued the principle of premature stranded cost recovery were really concerned about the dollars or promoting their individual competitive advantage as much as they were in principles. I conclude that the stranded costs in this case represent a fair and reasonable recovery in line with legislative intent and represent a reasonable "admission ticket" price for opening up the MPC system to full customer choice.   That reasonableness can be determined through the empirical test outlined in the order and the concurrence of some gas marketers, producers, Montana Consumer Counsel and competitors who do not share MPC's self interest in recovery. Those who would reject the plan and continue with business as usual would subject ratepayers to even ***greater*** stranded costs as these costs are presently in rates and would continue to be recovered for years from ratepayers under traditional regulatory standards. This settlement modifies full recovery and further outlines mitigation possibilities ***lessening*** ratepayer impacts rather than representing unfair recovery of investments made in a regulated environment.

While reaching the conclusion that the preponderance of evidence in this case shows conclusively that the settlements represent fair treatment of thorny issues involved in making the transition from a single supplier monopolistic business structure to a open market and competition regulated world, this Commissioner does not suggest that the arguments of Ferdig, Paladin, MHA, Enron and NMOGA were without merit. Contrary to allegations of self interest or greed as the sole motivating factor I found while their testimony may not have been entirely altruistic, they must be commended for the time, energy and considerable monetary resources they expended. Their presence as intervenors and potential spoilers surely influenced the outcome of negotiations between the parties and may have prompted major concessions from the applicant in critical issues like stranded cost recovery and rates. Further, their participation has prompted the Commission to include language in this order addressing some of their concerns. Their testimony will cast a long shadow as the Commission proceeds with rulemakings and related dockets to further effectuate the transition to customer choice.

Witness Jansky's testimony for Ferdig Oil presented powerful testimony that highlighted the dichotomy between the success and failure of regulation. His pointed testimony on his perceived failure of the Commission to force MPC to divest itself of out of market production carries credibility with the aid of perfect 20/20 hindsight. For the reasons outlined in the order, I believe the relief he suggests for denial of stranded costs is inappropriate and unfair. One must also recognize that regulation and MPC's own production at the time was hardly adverse to consumer interests as it sheltered consumers from high market prices which must also be viewed as a success of the monopoly structure and regulation. However, I believe Jansky's testimony does provide a compelling reason to adopt customer choice. Regulators have always conceded that their purpose was to act as a substitute for competition to restrain the ability of the monopoly to abuse customers. However well intended the regulator may be, I think Jansky illustrates that the regulatory process may be too slow and cumbersome and information too imperfect to achieve what a competitive marketplace could have provided for consumers. Faced with a declining market, cheaper sources of supply and competitors offering consumers better deals, I think it is reasonable to expect MPC would have been forced to do what Jansky suggested was reasonable.

Enron raised some interesting questions about whether the stipulation offer would encourage the development of a robust competitive marketplace. I concede his suggestions may result in such an outcome, but I believe the price extracted to reach that goal would have been too high for consumers. Regulators have a balancing act to follow-- promoting the development of competition ***and*** offering a measure of protection to remaining monopoly small users during the transition period. Adopting Enron's plan would have erred in favor of the former (competition) and subjected the latter (residential customers) to price increases foreclosed by the stipulation. Further, I believe their post transition plan calculation of stranded costs is incompatible with legislative intent and would force MPC to abandon its voluntary plan to further open its system to customer choice. It seems improbable to me that MPC would open its system without some recognition and recovery of costs that were incurred under the regulatory impact. Clearly, some recovery is an explicit cost of MPC's willingness to give up its captive customer base. This Commission can not be blind to its dual responsibilities. It is also apparent that the support (or lack of opposition) of other gas marketers and potential new entrants to the transition plan weakens Enron's arguments that the plan would solidify MPC's dominant role in the market and discourage competition. Enron largely stood alone in making its arguments.

However, in rejecting Enron's stranded cost position I believe witness Walsh has provided some valuable guidance in the establishment of rules to guide the new marketplace. I fully expect his comments to be very much in the forefront of future debates.

This Commissioner remains perplexed by the advocacy of MHA in this case. I am reminded of the suggestion the late Vermont Senator Aiken offered about a way to get the USA out of the Vietnam War. His sage advice was "To declare victory and go home." I think MHA would have been wise to do likewise. Their members are the most likely immediate beneficiary of the settlement. The ink was hardly dry on docket 90.1.1 when state hospitals beginning with St. James were appealing to the Commission for a lowering of the threshold level. The settlement will allow almost all MHA member hospitals access to competitive supply this winter. Unlike the USA in Vietnam, MHA is the winner in this settlement. For the reasons cited elsewhere in the order and my opinion I find their position on stranded costs untenable.

NMOGA testimony left this Commissioner on the horns of a dilemma. As the Commissioner from the district where NMOGA resides I would like to be able to support their positions but that representation of responsibilities collided with broader judicial responsibilities of a Commissioner. It is evident from my vote that the broader public interest and benefits of the stipulation were greater than the more parochial interests. Witnesses Perry and Coolidge have been aggressive advocates for producers and communities who will undoubtably face major impacts from this order. Yet is also evident that these producers are also presented with opportunities to become retailers to end customers rather than just wholesale suppliers to MPC. I believe the order is less than responsive to the issues raised by NMOGA and will briefly address them.

I am not unaware of the potential impacts on NMOGA's members. The discrepancies between the gas prices agreed to in the stipulation and the reality of market (ie. Canadian gas prices) and current Montana contracts will surely have adverse consequences on Montana producers. It would be an act of denial on the part of this Commission to not recognize that. Montana production may well be shut in and producers will face pressure to renegotiate their contracts downward resulting in the tax consequences predicted by NMOGA

NMOGA appears to recognize that the restructuring train was leaving the station and they finally softened their opposition to the stipulations if three conditions would be imposed by the Commission. Given the gravity of potential consequences on North Central Montana producers and taxing authorities I believe NMOGA deserves elaboration on why their compromise position offered in their initial brief cannot be imposed on the Commission at this time.

1. Stipulation Agreement Three, Item # 4, page 6. NMOGA asks the Commission to alter the purchase gas contract to divide prices and volumes between Montana and Canadian receipt points.

As many of the briefs of the parties point out this settlement was inclusive on most issues. The Commission has little latitude to alter such a settlement on issues of this magnitude without rejecting it in its entirety. This requested change is major.

However, it would be a disservice to hide behind the protection of a procedural blind- NMOGA deserves to have a response to the merits of their arguments and why the Commission found the condensed NMOGA offer unacceptable. NMOGA argued that this change would be harmless to ratepayers and they should be indifferent to the proposed amendment. My analysis is that such is not the case. MPC witness Perry Cole repeatedly testified during the hearing that MPC's ability to earn its authorized rate of return under the terms of the stipulation were solely independent on its ability to reduce costs to the tune of at least $3 million a year.

This Commission cannot ignore that testimony or its responsibilities. In a typical gas utility 70% or more of the utility cost of service is attributed to cost of supply. NMOGA has asked the Commission to remove from Montana Power its flexibility to control its major expense items from the efficiency mandate directed by the settlement.

Even if it were possible for the Commission to impose the requested condition one can guess it would have probably dealt a death blow to MPC voluntarily opening its system.

The Commission has an obligation to allow the utility to have an opportunity to earn its authorized rate of return. The condition requested by NMOGA would likely foreclose MPC's ability to do that in an open market and the best interests of the shareholders would be better served by remaining a closed utility and foreclosing what I perceive to substantial consumer benefits from competition. I must support the Commission's conclusion in its findings that the protectionist measure advocated by NMOGA denies MPC the flexibility it needs to manage its gas supply through the transition period to competition.

2. Stipulation Agreement Three, page 7, l4. Contract Assignability

NMOGA's appeal for a further condition on Contract Assignability is one I do sympathize with. Had NMOGA won that concession at the bargaining table I would have supported it. However, the merits of that position are not sufficient for this Commission to reject the settlement, risk MPC's withdrawing its offer to open its system or overcome the compelling testimony of MPC witness Cole that success of restructuring is dependent on MPC's ability to manage its gas supply. NMOGA was not able to prevail why its own interests were more compelling than the adoption of the stipulation.

3. Enforcement Penalties

> I support NMOGA's suggested penalties for violations of rules, however NMOGA is asking the Commission to bestow a power on itself that can only be given by the Legislature. The current penalty provisions through the district court are laborious, unduly adversarial and inappropriate to discourage unlawful conduct in a competitive marketplace that may attract unscrupulous operators. Having said that, I hope NMOGA will consider supporting or introducing permissive legislation in the 1999 Legislature.

While I am sympathetic to NMOGA's concerns no plan is perfect and the switch from regulated, single supplier monopoly paradigm will have down sides - not the least of which were identified by NMOGA. There will be consequences as the old order gives way to the new. There are significant impacts on tax policy and community impacts. A symbiotic business relationship that has existed for 50 years between producers and the company must be reshaped as they become both customers and competitors of each other. I believe the producers can respond to these challenges and the Commission must rightly reject their pleas for further accommodation as not being in the best interest of ratepayers generally. The Commission's language in the order cautioning MPC management to consider too abrupt changes which will impact producers and tax bases. The balancing act that is required is one of MPC's obligation in recognizing the transitional nature of the settlements. While NMOGA raised real issues they are insufficient for this Commission to reject the settlement and the broader public interest calls for this Commission to accept this stipulation rather than adopt the protectionist and parochial interests of one stakeholder in the industry.

One process question also deserves comment. I believe that this case illustrates the strength rather than the weakness of negotiated settlements. The business world today generally avoids litigation and employs it only as a case of last resort. They seek solutions to disputes through principled compromises and negotiated settlements. The utility and regulatory sector was slow to adopt this stance, but I continue to maintain that such settlements, where many competing interests arrive at an acceptable outcome, represent a better outcome than the traditional "winner take all" posturing of a contested rate case where the regulator is left to make all the decisions. The concurrence of so many diverse economic interests in support of the stipulation leads me to conclude they do approach the proverbial "win/win" desired outcome of principled negotiation. While I sympathize with NMOGA's pleadings that the PSC is the only party that can evaluate broad public interests, I believe the challenge is to find a way to include PSC staff a role in future negotiated settlements rather than discourage settlements. Ideas that might come to mind is the use of Commission directed settlement principles or the formulation of a MPSC policy unit to participate in settlements.

In endorsing these stipulations, I believe it lays a foundation and path for full customer choice that is in the public interest. Yet, I recognize that much work remains to be done to insure ratepayer protection and encourage the development of robust competition. As such I support comprehensive rulemaking on issues that remain open or only partially resolved by this docket. Issues like anti-competitive business practices, quality of service rules and consumer protections need to be fleshed out and discussed in rulemakings. The Commission itself must reorganize itself to be more responsive to its altered responsibilities in the new utility operating environment.

In conclusion, this Commissioner finds that full customer choice is in the public interest and the stipulation package does offer sufficient protections and details to merit approval by the Commission. I must note, however, that regulation and the monopoly structure has not been a failure. It has resulted in unparralled quality of service, protection from market price swings, societal benefits such as low income protection and conservation efforts to name a few. The challenge of regulation is to not preserve itself or traditional structures through maintaining the status quo, but to look for ways to preserve the benefits regulation has offered even in a competitive environment. Where that may not be possible in a competitive environment, I believe the benefits of competition still outweigh any benefit losses. For example, even before small residential customers gain the right to choose suppliers I believe they will accrue substantial benefits. Not the least of which will be the transformed utility manager mind set who now will have to fight for market share to preserve profits rather than depending on a captive customer list and sympathetic regulators and courts. To survive in a competitive environment, the utility will no longer resort to drowning the regulator in costly studies and expert testimony but rather from offering customers a competitive price and product that better meets the customer needs.

In approving this order the Commission has made a historic decision. The questions I posed earlier appear to be answered by the evidence. The stipulations appear to be in the public interest. The threshold level is reduced immediately with a timetable for full customer choice, residential rates will fall, supply costs will decline for 5 years, stranded cost recovery is reasonable and some societal benefits have been assured. No party was able to convincingly show why their position was suitable to the compromise settlement offered by a majority of the intervenors. Only time will conclusively prove whether it is correct, but based on the evidence I believe the terms and conditions contained in the stipulations represent sound and balanced public policy. On November 1st, MPC must compete for the revenues from a significant portion of their customer base. By the year 2002 (and before, if I have my way based on anticipated positive results of the pilot projects) all customers will have an opportunity denied to them for several generations- the right to choose their own natural gas supplier best suited to their own needs.

The time for words is over....now is the time for action. The public debate has forged a reasonable solution. I support the adoption of new market forces as a positive and pro-consumer change which will deliver significant benefits to the state of Montana and the customers of MPC's natural gas utility. I applaud and endorse the hard work of the parties and the compromises they made at the bargaining table so that this reform and new opportunities might proceed, at least in part, for this winter heating season.

Those opponents of MPC who fought for decades to allow customer choice through the old "PUD" debates in the Legislature, can take heart with this order. However belated, their effort has been vindicated and the battle won. Little did they ever dream it would be Montana Power to make the proposal voluntarily. With this order, consumers are assured the right to choose their natural gas supplier.

RESPECTFULLY SUBMITTED this 31st day of October, 1997.

DANNY OBERG
Commissioner

Opinion of Commissioner Rowe
MPC Natural Gas Docket 96.2.22, Order No. 5898d

The Commission has under consideration several additional stipulations as it moves toward implementing competition in the provision of natural gas supply. Because of the limitations in the record before us, the choices are difficult. No option is fully satisfactory. The challenge is to reach an outcome which is grounded in the record and will achieve good public policy, while being consistent with Legislative direction in Senate Bill 396.

The Commission may approve the stipulations (along with some additional directions, qualifications, and limitations) or reject the stipulations. If it rejects the stipulations, it must either dismiss the case or take it to hearing for the parties now supporting the stipulations to present more complete cases. Approving the stipulations means accepting certain very troubling terms, especially those concerning stranded costs. Rejecting the stipulations means significantly postponing the introduction of supply competition for medium-sized loads.

At the June 20, 1997 stipulation presentation, I asked the parties to address a series of issues. Among proponents of the stipulations, MPC made a particular effort to do so. It offered additional information on affiliate structure and other matters which went some way to addressing my concerns. The stipulations offer a number of good elements, including specific recognition of the customers' contribution to the value of assets which might eventually be sold at greater than book value, an issue of long-standing concern to the Montana Consumer Counsel. The stipulations also offer many elements of a road map toward retail competition.

However, parties opposing the stipulations raised several very serious objections, some of which could cause real concern should the Commission's order be appealed. My primary concerns fall into two categories, affiliate interest considerations and stranded costs.

Affiliate interest concerns involve transactions between the non-competitive core unit and the competitive supply unit. Getting the rules right is essential to protect customers of the core from assuming greater risk or cost than appropriate, and also to protect competitors of the supply unit from unfair competition. Unfairness may result from a variety of sources, such as shifting resources to the competitive side, taking advantage of superior access to information, or even continued use of a well-established company name by the competitive unit (brand loyalty or a first-mover advantage). MPC established that it had gone some way to address these concerns. Opponents established that significant concerns still remain. Without violating the stipulations, the Commission has only limited ability in this docket to address these issues. I hope that it may do more and better in future rulemaking.

By far the most troubling aspect of the stipulations concerns stranded costs. Section 69-3-1402(9)(a) makes clear that to be recoverable from ratepayers, these “transition costs” must be “net, verifiable” costs which “become unrecoverable as a result of customer choice and open access.” The stipulating parties maintain that discovery conducted in the docket constitutes sufficient verification, and that the costs will in the future be stranded as the system moves to competition. They have a colorable argument. However, a strong argument may be made that costs proposed to be recovered are not adequately verified and that not all costs proposed to be recovered are “unrecoverable as a result of customer choice and open access,” particularly those costs associated with core customers who are not yet moving to competitive supply. A hearing in which all parties squarely addressed these issues through development of a detailed, factual record would have been a vastly superior way to address these matters.

The hearing produced additional stranded cost questions, such as the logic behind exempting certain new loads from stranded cost recovery while not exempting others. None of these questions may be adequately addressed without violating the stipulations.

Stipulations are important and useful. Stipulations may settle routine issues. They may narrow the range of disputed issues in a complex case. They may confer additional choices to a decision-maker, consistent with an evidentiary record (as did the gas contract stipulation in MPC Docket 90.1.1 and the local measured service stipulation in U S WEST Docket 95.10.146).

I voted for the earlier stipulations in this docket with no reservation. Here, however, opponent parties mounted substantial factual and legal challenges. Rather than crafting the best overall solution based on a complete record, the Commission has a brittle, binary choice between two suboptimal approaches.

I pledge to work with all the parties to make the new regime work. I sincerely hope that it will.

I ask all parties to avoid placing the Commission in a similar position as we continue work on the even more complex electric supply restructuring process. Working with the various parties and within the legislative framework, the Commission must be able to craft outcomes in that process which are best for our citizens, best for the economy, and best for Montana.

RESPECTFULLY SUBMITTED this 31st day of October, 1997.

BOB ROWE
Commissioner